Supreme Court of the United States.

OCTOBER TERM, 1977.

No. 77-3341

FIRST FEDERAL SAVINGS AND LOAN ASSOCIATION OF BOSTON, ET AL.,
APPELLANTS,
v.
STATE TAX COMMISSION, ET AL.,
APPELLEES.

ON APPEAL FROM THE SUPREME JUDICIAL COURT OF MASSACHUSETTS.

Jurisdictional Statement.

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Jurisdictional Statement.

This is an appeal brought by all of the Federal savings and loan associations of Massachusetts (the "Associations") from a decision of the Supreme Judicial Court of Massachusetts upholding the validity of a Massachusetts statute imposing a tax on each of the Associations.

The Supreme Judicial Court of Massachusetts held that Massachusetts did not exceed the authority to tax Federal savings and loan associations granted by Congress to the states under 12 U.S.C. § 1464(h) despite its finding that the tax imposed discriminates in favor of Massachusetts-chartered institutions. The Court designated the Federal Home Loan Bank Board as the source

of the discrimination, not the Commonwealth. The test imposed by the Massachusetts Court requires the Federal instrumentalities to show they are at a "substantial competitive disadvantage" in order to invalidate the tax. Such a standard conflicts with that established by this Court in *Laurens Federal Savings & Loan Assn.* v. *South Carolina Tax Commission*, 365 U.S. 517, 523 (1961), in which this Court stated that 12 U.S.C. § 1464(h) "unequivocally bars discriminatory state taxation of the Federal Savings and Loan Associations." The Massachusetts Court also rejected the Associations' argument that the tax in question resulted in discrimination prohibited by the Federal statute because of the exemption of Massachusetts credit unions and rejected the argument that the tax in question was not imposed on a subject of taxation permitted under the Federal statute.

Finally, the Massachusetts Court rejected the contention by the Associations that the taxing statute as applied to them was in violation of the Commerce Clause and the Due Process and Equal Protection Clauses of the Fourteenth Amendment to the United States Constitution.

To permit these holdings of the Supreme Judicial Court of Massachusetts to stand is likely to have significant impact on taxing policies toward Federal savings and loan associations in all states.

Opinion Below.

The opinion of the Supreme Judicial Court of Massachusetts is reported at Mass. Adv. Sh. (1977) 895, 363 N.E. 2d 474, and is set forth in Appendix A.

Jurisdiction.

On April 16, 1975, Appellants filed a Complaint for Declaratory Relief in the Superior Court for the County

of Suffolk, Commonwealth of Massachusetts, in which they sought declarations that the Massachusetts statute imposing a tax on Federal savings and loan associations, Massachusetts G.L. c. 63, §§ 11(*a*)(1) and 11(*b*)(1), was invalid and unenforceable as applied to such associations on the grounds that it: (a) was outside the scope of the authority granted by Congress to the states in 12 U.S.C. § 1464(h) to tax such Federal instrumentalities, (b) violated the Due Process and Equal Protection Clauses of the Fourteenth Amendment to the U. S. Constitution, and (c) violated the Commerce Clause of the United States Constitution and on various State statutory and constitutional grounds.

The Superior Court reserved and reported the case on a record consisting of the pleadings, a stipulation of facts, and an affidavit in support of Appellants' motion for summary judgment. The Supreme Judicial Court of Massachusetts granted Appellants' request for direct appellate review. On May 3, 1977, the Supreme Judicial Court entered a final judgment ordering that a declaratory judgment be entered in the Superior Court for the County of Suffolk, upholding the validity of the State statute in all respects. A Notice of Appeal to this Court was filed in the Supreme Judicial Court of Massachusetts on July 20, 1977. The Notice of Appeal is set forth in Appendix B.

The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1257(2). Since the Supreme Judicial Court of Massachusetts upheld the validity of a State statute which had been drawn in question on the ground of its being repugnant to the Constitution and laws of the United States, this matter is appropriately brought to this Court by appeal. *See, e.g., Warren Trading Post Co.* v. *Arizona Tax Commission*, 380 U.S. 685 (1965); *American Oil Co.* v. *Neill*, 380 U.S. 451 (1965).

The statutory provisions the validity of which is involved herein are Massachusetts G.L. c. 63, §§ 11(*a*)(1) and 11(*b*)(1), which provisions, together with a definition also found in said § 11, are set forth in Appendix C.

If this Court does not consider appeal to be the proper method of review, the Appellants request that this document be treated as a petition for writ of certiorari pursuant to 28 U.S.C. §§ 1257(3) and 2103.

Questions Presented.

Under § 5(h) of the Home Owners' Loan Act of 1933, 12 U.S.C. § 1464(h), states may not impose a tax on Federal savings and loan associations or "their franchise, capital, reserves, surplus, loans, or income greater than that imposed . . . on other similar local mutual or cooperative thrift and home financing institutions."

Massachusetts imposes a tax measured in part by deposits and in part by "net operating income" on Federal associations and on certain local thrift institutions. Massachusetts credit unions are exempt from the tax. In arriving at "net operating income" a deduction is allowed for "operating expenses." No deduction is allowed for interest or dividends paid to members of a savings and loan association. A deduction is allowed for "minimum additions . . . to its guaranty fund or surplus required by law or the appropriate federal and state supervisory authorities." Since Federal savings and loan associations are subject to lower surplus requirements, their allowable deductions are less than those available to Massachusetts-chartered cooperative and savings banks and their income subject to tax is thus greater.

The questions which result are:

1. Does 12 U.S.C. § 1464(h) prohibit the acknowledged discrimination in favor of Massachusetts institutions which results from the allowance of deductions for minimum required additions to guaranty fund or surplus?

2. Are Massachusetts credit unions, which are conceded to be "local mutual or cooperative thrift and home financing institutions," "similar" to Federal savings and loan associations under 12 U.S.C. § 1464(h)?

(a) Is "similarity" to be judged by the statutory powers of the two kinds of entities?

(b) Is "similarity" to be judged by the presence or absence of factual competition? If so, is such competition to be measured collectively or by an individual comparison?

(c) If the proper test is statutory powers, are the powers of such entities "similar?"

(d) If the proper test is factual competition, have Appellants established competition collectively and individually?

3. Is the tax imposed on "net operating income" authorized by 12 U.S.C. § 1464(h)?

4. Does the Massachusetts statute violate the Commerce Clause of the United States Constitution by its failure to provide for allocation or apportionment of income to other states?

5. Does the use of separate and unequal standards for measuring deductions for required additions to guaranty fund or surplus result in violation of the Due Process and Equal Protection Clauses of the Fourteenth Amendment to the United States Constitution?

Statement of the Case.

Appellants are Federal savings and loan associations which are chartered pursuant to 12 U.S.C. §§ 1461-1468, and each is a member of the Federal Home Loan Bank System pursuant to 12 U.S.C. §§ 1421-1429. Collectively, the Appellants constitute all of the chartered Federal savings and loan associations located within the Commonwealth of Massachusetts. Although located within the Commonwealth, the Appellants derive substantial income from mortgage loans and participations with respect to real estate outside Massachusetts. Appellants are all located within 100 miles of another state, and at least one appellant is located in a city on the border of Connecticut, Maine, New Hampshire, New York and Rhode Island.

The Federal statute authorizing state taxation of Federal savings and loan associations provides:

> No State . . . shall impose any tax on such associations or their franchise, capital, reserves, surplus, loans, or income greater than that imposed by such authority on other similar local mutual or cooperative thrift and home financing institutions.
>
> 12 U.S.C. § 1464(h).

In 1966, Massachusetts enacted § 11 of Chapter 63 of the Massachusetts General Laws, imposing a tax on all Federal savings and loan associations located in the Commonwealth and on State-chartered savings banks and cooperative banks, but not on Massachusetts credit unions. A tax is imposed on "net operating income" (§§ 11(*a*)(1) and 11(*b*)(1)) and on deposits (§§ 11(*a*)(2) and 11(*b*)(2)). The deposits tax is imposed semiannually, returns being required in July and January, while the income-based tax is an annual tax. The critical provisions of the income-based portion of the Massachusetts statute are that (1) no deduction is allowed for payments to depositors in arriving at net operating income despite the fact that such payments represent, by a large measure, the principal cost of operations, and (2) deductions from net operating income are allowed for

> minimum additions during the taxable years to . . . [the] guaranty fund or surplus required by law or the appropriate federal and state supervisory authorities . . . .
>
> Mass. G.L. c. 63, § 11(*iii*).

A Massachusetts cooperative bank must set aside into a guaranty fund 10% of its assets at the rate of 5% of net profits per year. Mass. G.L. c. 170, § 38. A Massachusetts savings bank must set aside 7½% of deposits at the rate of ⅛ to ¼ of 1 percent of total deposits. Mass. G.L. c. 168, § 58. By contrast Federal associations are required to set aside only 5% of insured accounts, which requirement must be met within twenty years or, if mortgage needs so require, within thirty years. 12 U.S.C. § 1726(b). The rate of additions is determined by the Federal Savings and Loan Insurance Corporation, which is subject to the Federal Home Loan Bank Board. The Massachusetts Supreme Judicial Court found that the effect of the above difference in reserve requirements was adversely discriminatory to the Federal associations but not repugnant to § 1464(h). Mass. Adv. Sh. (1977) at 909, 363 N.E. 2d 474, 484.

A table comparing the statutory powers of Federal savings and loan associations, Massachusetts credit unions, Massachusetts cooperative banks and Massachusetts savings banks is set forth in Appendix D.

Appellants paid the taxes imposed by c. 63, § 11, but for various assessment periods some or all of them protested the assessment of the tax and filed applications for abatement in accordance with Mass. G.L. c. 63, §§ 18A and 51. After denial of the applications for abatement, the

United States, on behalf of the Appellants, challenged the deposits element of the tax on several statutory and State and Federal constitutional grounds by seeking declaratory relief in the Federal District Court for the District of Massachusetts. The District Court held the deposits element of the tax to be in violation of 12 U.S.C. § 1464(h) and the Supremacy Clause. *United States* v. *State Tax Commission*, 348 F. Supp. 397, 400 (D. Mass. 1972). The Court of Appeals affirmed the holding on the exclusive ground that the tax was discriminatory. *United States* v. *State Tax Commission*, 481 F. 2d 963, 970 (1st Cir. 1973). The opinion of the Court of Appeals is set forth in Appendix E.

Some of the Appellants intervened in the Federal court litigation in order to challenge the net operating income element of the tax, but the Court of Appeals held that a challenge to that portion of the tax (§§ 11(*a*)(1) and 11(*b*)(1)) could more appropriately be decided in a State forum. The Appellants commenced an action for declaratory relief in the Suffolk (Massachusetts) Superior Court on April 16, 1975 and stayed proceedings which had been commenced before the Appellate Tax Board of the Commonwealth. On December 24, 1975, the parties agreed in writing as to all the material facts in the case and filed motions for summary judgment. Prior to a decision with respect to those motions, and at the request of all parties, the Superior Court judge reported the case without decision to the Appeals Court on January 30, 1976, pursuant to Mass. G.L. c. 231, § 111. An appeal was entered in the Appeals Court on March 12, 1976. On March 29, 1976, Appellants applied in writing to the Supreme Judicial Court for direct review, which application was granted on April 15, 1976. Briefs were submitted and oral argument held, and on May 3, 1977, the Supreme Judicial Court issued a decision rejecting all of Appellants' challenges to

the tax on income and holding Mass. G.L. c. 63, §§ 11(*a*)(1) and 11(*b*)(1) not to be in violation of either 12 U.S.C. § 1464(h) or the Federal Constitution. *First Federal Savings and Loan Association* v. *State Tax Commission*, Mass. Adv. Sh. (1977) 895, 363 N.E. 2d 474.

The Federal questions raised in this appeal from the decision of the Massachusetts Supreme Judicial Court were all raised in the initial Complaint for Declaratory Relief. In paragraphs 82, 85, and 88 thereof the Appellants asserted that the tax imposed by the Massachusetts statute is not a tax authorized by 12 U.S.C. § 1464(h). In paragraph 110 they alleged that the failure to extend the tax to Massachusetts credit unions renders it discriminatory in violation of 12 U.S.C. § 1464(h). In paragraphs 102 and 94, respectively, they alleged violations of the Commerce Clause and the Due Process and Equal Protection Clauses of the Fourteenth Amendment to the United States Constitution. The prayers for relief sought declarations that the Massachusetts statute was invalid for all the foregoing reasons. Because the case was reserved and reported from the Superior Court directly to the Appeals Court and the Supreme Judicial Court subsequently granted a request for direct review, these issues were all properly before the Supreme Judicial Court.

The Supreme Judicial Court considered each of the Federal issues separately and sustained the validity of the Massachusetts statute in all respects.

With respect to the 12 U.S.C. § 1464(h) issues, the Court stated:

> We think that the purpose of § 1464(h) is not frustrated by the circumstance that reserve or guaranty fund requirements differ. The cause of the discrimination is the lower requirements imposed by the Federal regulatory agency on Federal savings and loan asso-

ciations. The Commonwealth is not the source of the discrimination. The excise statute is wholly neutral.

> Mass. Adv. Sh. (1977) at 909, 363 N.E. 2d 474, 482.

It also stated:

> The test for similarity [of credit unions and Federal savings and loan associations] is not what each type of institution might do but rather what each does in fact . . . . The proper method of measuring similarity may be a collective, rather than an individual, comparison.
>
> *Id.* at 913, 914, 363 N.E. 2d 474, 484.

Despite its finding that approximately 42% of credit union loans were in real estate mortgages, the Court found a failure of proof that "credit unions compete substantially . . . for the same types of investors and the same class of borrowers." *Id.* at 914, 363 N.E. 2d at 484. Hence it held that failure to tax credit unions did not lead to discrimination against Federal savings and loan associations in violation of 12 U.S.C. § 1464(h). The Court did not comment on the fact that at least one credit union had over 80% of its assets invested in real estate mortgage loans.

With respect to the Commerce Clause issue, the Supreme Judicial Court stated:

> The record shows that collectively the associations invest a substantial portion of their funds (about 29% in 1974) in mortgage loans secured by real estate located in other States. The record does not show the extent of the contacts of any association with any other State nor does it show whether, in the circumstances of its business operations, any other State does or could impose a tax or excise on any association. Of course, no other State could impose an excise on an association's privilege to do business in Massachusetts. . . . Even if we assume, as the associations argue, that the issue of burdening interstate commerce turns on what other States may do, and not what they do in fact, the associations have not met their burden of establishing that § 11 improperly imposes on interstate commerce. The record is devoid of any information with respect to the contacts and activities of any individual Federal savings and loan association in any other jurisdiction.

> *Id.* at 907-908, 363 N.E. 2d 474, 481 (citations omitted).

With respect to the Due Process and Equal Protection arguments, the Supreme Judicial Court stated:

> . . . [E]ven if we were to accept the assertion that the associations are placed in a separate class (because of the action of an agency of the Federal government), such a classification would not be impermissible. Legislative classifications for tax purposes are given wide respect in the face of constitutional challenges.
>
> *Id.* at 910, 363 N.E. 2d 474, 482-483.

The Federal Questions Presented Are Substantial.

A. The Massachusetts Statute Discriminates Against Federal Savings and Loan Associations both Individually and Collectively.

Massachusetts permits a deduction in determining net operating income for required additions to an institution's guaranty fund or surplus. Massachusetts cooperative banks are required to reserve 10% of assets at the rate of

5% of net profits annually. Mass. G.L. c. 170, § 38. Massachusetts savings banks are required to reserve 7½% of deposits at the rate of ⅛ to ¼ of 1% of deposits annually. Mass. G.L. c. 168, § 58. Federal associations are required to reserve only 5% of insured accounts; the rate of addition is governed by the Federal Home Loan Bank Board but must reach 5% of insured accounts within 20 years, or, under special circumstances, within 30 years. 12 U.S.C. § 1726(b). The rate of addition to guaranty funds or surplus has resulted in larger deductions and lesser taxes for the State institutions. The Supreme Judicial Court acknowledged the existence of this adverse discriminatory treatment of Federal associations collectively in the following terms:

> [W]e accept the [Federal] associations' assertion that, generally, the required contributions of a Federal savings and loan association to its surplus are less than those of similarly situated Massachusetts savings and coöperative banks.
>
> Mass. Adv. Sh. (1977) at 909, 363 N.E. 2d 474, 482.

The Massachusetts Court failed to comment upon the demonstrated adverse individual discrimination which results from the dual standard for deductions for required additions to reserves, brought to its attention in the following language:

> The First Federal Savings and Loan Association provides a specific illustration of this type of discriminatory effect of c. 63, § 11. From 1970 to 1971 total deposits in the First Federal Savings and Loan Association grew from $75,101,331 to $79,975,993. At the end of the fiscal year terminated October 31, 1971, the North Attleborough Savings Bank had total deposits

> of $72,924,597 and the Milton Savings Bank had total deposits of $74,315,812. The former was required to transfer $174,500 to its guaranty fund and the latter $185,000, and each was entitled to a c. 63, § 11 deduction in the corresponding amount. However, the First Federal Savings and Loan Association was not required to set aside any reserve funds and thus did not qualify for a deduction, despite the fact that it did voluntarily transfer amounts to its reserve accounts.
>
> Brief to the Supreme Judicial Court of Massachusetts 32 (citations omitted).

Thus, the problem of whether § 1464(h) is to be construed on the basis of an individual or collective comparison was avoided by Appellants by demonstrating discrimination at both levels. The Court chose to nullify the effect of the discrimination. It stated:

> The cause of the discrimination is the lower requirements imposed by the Federal regulatory agency on Federal savings and loan associations. The Commonwealth is not the source of the discrimination.
>
> Mass. Adv. Sh. (1977) at 909, 363 N.E. 2d 474, 482.
>
> The operation of § 11 in conjunction with the less strict reserve requirements applicable to Federal savings and loan associations has not been shown to present a substantial competitive disadvantage.
>
> *Id.*

It is submitted that the source of adverse discriminatory tax treatment is an irrelevant inquiry. The plain wording of § 1464(h) is that no tax may be imposed on Federal associations "greater than" is imposed on local institutions. This Court has stated that § 1464(h) "unequivo-

cally bars discriminatory state taxation of Federal Savings and Loan Associations." *Laurens Federal Savings and Loan Association* v. *South Carolina Tax Commission*, 365 U.S. 517, 523 (1961). It having been established that the tax on Federal associations is greater, the State statute must fall. There should be no necessity to prove the extent of the "competitive disadvantage" which results. Further, the Federal statute imposes no tax; only the Massachusetts statute does that. Accordingly, the Massachusetts Court's conclusion that the Commonwealth is not the source of the discrimination is not supportable. The Massachusetts Court chose not to refer to the opinion of this Court in *Laurens*, despite its controlling effect.

Moreover, a review of the history of the deduction for additions to reserves supports the view that deliberately discriminatory treatment of Federal associations was intended parallel to that involved in the tax on out-of-state loans imposed by §§ 11(*a*)(2)(ii) and (*b*)(2)(ii) which was condemned by the Court of Appeals in *United States* v. *State Tax Commission*, 481 F. 2d 963 (1st Cir. 1973). The amount of, and rate of, addition to the reserves required for Massachusetts cooperative and savings banks were fixed by statute prior to the 1966 enactment of § 11, as was the amount of the reserve requirement for Federal associations. There is no reason to believe that the legislature acted out of ignorance rather than with knowledge of its own enactments. The legislature must have known the rates of addition and ultimate amounts of the reserves required of local institutions by statute. It is more probable that the legislature deliberately attempted to provide tax reductions for local institutions either as a distinct benefit or as an offset to possible competitive disadvantages which local institutions might incur by reason of more stringent reserve requirements imposed by local statutes. As the Court of Appeals said:

> Federal associations are entitled not to be singled out for special tax burdens; and it makes no difference whether the latter are expressly written into the statute or are tailored, as here, more subtly.
>
> 481 F. 2d at 970.

It might be argued, as the Massachusetts Court suggests, that the Federal Home Loan Bank Board could, by accelerating the rate of required contributions by Federal associations to reserves, reduce, eliminate or reverse the discriminatory tax result for one or more years. For example, if the eventual 5% of insured accounts reserve requirement for Federal associations were fixed as a requirement by the Federal Home Loan Bank Board to be met in one year's time rather than over 20 years, the Federal associations probably would have a larger deduction, in the one year, than the State institutions. The argument fails, however, since the larger reserve requirement of State institutions will necessarily provide larger total deductions eventually. In the case of Massachusetts cooperative banks, the deductions in time will be more than twice those of a comparable Federal association.

More importantly, the power conferred upon the Federal Home Loan Bank Board to regulate the rate of addition to reserves of Federal associations is obviously designed to advance the national purposes of promotion of thrift, safety, and the regulation of the supply and flow of funds for home financing. The power clearly was not conferred to neutralize discriminatory state taxing policy; that result is mandated by § 1464(h). It should be noted that the Federal Home Loan Bank Board has employed its power to alter or suspend additions to reserves on a number of occasions, while Congress extended to 30 years the period in which to satisfy the reserve require-

ment, if "necessary to meet mortgage needs," in the Emergency Home Finance Act of 1970.

Rather than view the *Laurens* case as controlling, the Massachusetts Court imposed, as a test of discriminatory tax treatment, the necessity of a showing by the Federal associations that they were at "a substantial competitive disadvantage." The test is alien to the judgment of this Court in *Laurens*.

The Massachusetts Court also asserted:

> Because of lower reserve requirements, Federal associations tend to have more funds available for immediate distribution to members than similarly situated State institutions.
>
> Mass. Adv. Sh. (1977) at 909, 363 N.E. 2d 474, 482.

The assertion is pure speculation and is contrary to fact. The record is devoid of evidence concerning the relative dividend paying capacity of the types of institutions. Moreover, permissible dividends are primarily a function of action by appropriate regulatory authorities. For example, in 1971, the Massachusetts Bank Commissioner authorized State-chartered banks to pay 5.25% interest on regular savings accounts at a time when Federal associations were limited to 5%. In order to remain competitive, the Federal Home Loan Bank Board made an exception to its nationwide interest limitation of 5%, authorizing a rate of 5.25% for its Massachusetts members.

B. Massachusetts Credit Unions Are Mutual Thrift and Home Financing Institutions Similar to Federal Savings and Loan Associations.

That Massachusetts credit unions are "local mutual or cooperative thrift and home financing institutions" has been conceded. *See* Mass. Adv. Sh. (1977) at 912, 363 N.E. 2d 474, 483. The issue here is what standard should be used to determine whether credit unions are "similar" to Federal savings and loan associations within the meaning of 12 U.S.C. § 1464(h) and whether the standard has been met.

The Associations urge that the proper standard of comparison is the statutory powers conferred upon the two kinds of entities. The Massachusetts Court rejected this standard, stating: "The test for similarity is not what each type of institution might do but rather what each does in fact . . . ." Mass. Adv. Sh. (1977) at 913, 363 N.E. 2d 474, 484. In so holding, the Court failed to distinguish the opinion of this Court in *Morrissey* v. *Commissioner*, 296 U.S. 344 (1935), the leading case on classification of entities as associations taxable as corporations, trusts, or partnerships under the Internal Revenue Code.

In *Morrissey*, a trust with transferable shares had been created to develop a tract of land through the improvement and sale of a portion of the tract and to construct a golf course on the balance of the land. All sales activity had been completed prior to the beginning of the tax years before the Court. The trustees argued that the absence of business activities in the years before the Court should be taken as evidence of the character of the trust. This Court rejected the test of "what each does in fact," imposed here by the Massachusetts Court, adopting instead the test of "what each type of institution might do." It stated:

> The fact that these sales were made before the beginning of the tax years here in question . . . did not alter the character of the organization. *Its character was determined by the terms of the trust instrument.* . . . The powers conferred on the trustees con-

tinued and could be exercised for such activities as the instrument authorized.

296 U.S. at 361 (emphasis added).

Massachusetts credit unions are permitted to engage in substantial home financing, being authorized to invest up to 80% of the sum of their shares, deposits, guaranty fund, reserve fund and undivided earnings in real estate mortgage loans upon terms substantially identical to those authorized for Federal associations. Mass. G.L. c. 171, § 24(*b*)(7). Unlike Federal credit unions, there is no restriction on membership in either type of entity, and members of both are entitled to vote. Mass. G.L. c. 171, § 13. The two areas of principal dissimilarity between Massachusetts credit unions and Federal associations are (1) credit unions may pay 8% interest on deposits while Federal associations are limited to 5.25% and (2) credit unions are admonished by statute to give preference to personal loans while Federal associations are not. However, no method of enforcement for the latter provision is prescribed. Under 12 U.S.C. § 1464(h), the "local mutual or cooperative thrift and home financing institutions" to which Federal associations must be compared need only be "similar," not identical. Massachusetts credit unions are limited by statute to dealing with the individual, non-commercial depositor and borrower, whose business they share with Federal associations. Their statutory powers allow them to appeal to such customers by offering the the same basic types of financial services as do such associations.

Rejecting the statutory powers test in favor of a factual inquiry, the Massachusetts Court concluded that:

> The associations have not shown that credit unions compete substantially with Federal savings and loan associations for the same types of investors and the same class of borrowers. Nor have they shown the extent, if any, to which credit unions and Federal savings and loan associations are in direct competition with each other.
>
> Mass. Adv. Sh. (1977) at 914, 363 N.E. 2d 474, 484.

That conclusion is wrong. In 1972, credit unions, in the aggregate, had approximately 42% of their total loans in real estate mortgages. Mass. Adv. Sh. (1977) at 914. That Federal associations had larger percentages so committed does not rebut this evidence of real and substantial competition. Individually, more than twenty credit unions had more than 50% of their total assets invested in real estate loans, with one credit union investing 86.3% of its assets in real estate loans in 1973. Massachusetts credit unions held assets approximately equal to ½ those held by Federal associations. Annual Report of Massachusetts Commissioner of Banks for 1973, § B.

If the statutory powers of Massachusetts credit unions and Federal associations are to be compared in judging similarity of the two kinds of entities, relief should be granted to the Federal associations. If, instead, the proper standard of comparison is what the two kinds of entities actually do, either collectively or individually, the evidence shows substantial competition on both an individual and a collective basis, thus justifying the relief sought.

C. The Tax Imposed on Net Operating Income of Federal Associations Is Not an "Income" or "Franchise" Tax within the Meaning of 12 U.S.C. § 1464(h) and Does Not Otherwise Conform with the Federal Statute.

The fundamental error in the decision of the Massachusetts Court is the apparent view that the Federal limita-

tion on a state's authority to tax is simply that no greater tax may be imposed on Federal associations than is imposed on local institutions. That view assumes that the enumerated bases of taxation, *viz.*, "franchise, capital, reserves, surplus, loans, or income," are merely illustrative of, rather than limitations on, the permitted subjects of taxation.

It may be noted that the Massachusetts Court characterized the tax imposed by Mass. G.L. c. 63, § 11 as a franchise tax while the U. S. Court of Appeals treated the taxes imposed under § 11 as two separate taxes. The Court of Appeals characterized the taxes imposed as an income tax and a deposits tax, invalidating the latter and leaving the former to be challenged in the State courts. Presumably, the characterization as an income or franchise tax, or otherwise, is properly made under the Federal statute.

While § 11 provides a deduction for operating expenses in determining "net operating income," the amount on which the tax is levied, the Massachusetts Court held that ". . . dividends and interest paid to members are not [deductible] 'operating expenses' . . . ." Mass. Adv. Sh. (1977) at 903, 363 N.E. 2d 474, 480. "Net operating income," so defined, does not conform to the longstanding definition of income of Federal associations for Federal income tax purposes. Dividends and interest paid to members are deductible under I.R.C. § 591. Additionally, this Court has analogized deposits in Federal associations with checking accounts, concluding that such deposits "actually retain the qualities of money," and are not permanent investments because they are not speculative and may be readily withdrawn. *Porter* v. *Aetna Casualty & Surety Co.*, 370 U.S. 159, 161-162 (1962). There should be no question under current concepts of Federal taxation that

this cost of retaining old deposits and attracting new deposits would be deductible as interest. *See* 4A Mertens, *Law of Federal Income Taxation*, §§ 26.10 and 26.04 (1972). Refusal to allow a deduction for interest payments on deposits precludes classification of the excise as an income tax within the meaning of § 1464(h).

Additionally, use of the deduction for additions to guaranty funds or surplus precludes characterization of the tax as one levied on income. Minimum additions to surplus or guaranty funds are irrelevant to a determination of income. Accounting Research Bulletin No. 43, c. 8, ¶12(b). Reserves are merely bookkeeping entries which are reflected on the balance sheet, not the income statement. Loss reserves are the total accumulation required to meet losses and are not a measure of the rate at which losses are sustained, and it is only the latter which are a measure of income. Such reserves are not a measure of income; they are neither amounts paid nor are they an estimate of expenses. Income cannot be determined by a factor which is in no way a measure of income.

If, instead, the Massachusetts excise is properly characterized as a franchise tax, as it was described by the Massachusetts Court, it still must fail since a franchise tax must properly reflect the value of the exercise of the Federal charter in the Commonwealth of Massachusetts. Provision must be made for exclusion from State taxation of income not attributable to Massachusetts. *State Tax Commission* v. *John H. Breck, Inc.*, 336 Mass. 277, 144 N.E. 2d 87 (1957). The record discloses that approximately 35% of the income of the Associations for the years involved was derived from loans secured by real estate outside the Commonwealth (R. 234). It is inconceivable that a statute which fails to provide for any apportion-

ment of income outside the Commonwealth under such circumstances could possibly accurately measure the value of the exercise of the franchise in the Commonwealth. *See Complete Auto Transit, Inc.* v. *Brady*, 45 U.S.L.W. 4259 (March 7, 1977).

Finally, § 11 is violative of 12 U.S.C. § 1464(h) simply because it provides for two different and unequal measures of tax for the State and Federal institutions. It is of no consequence whether the statute is, as the Massachusetts Court described it, "wholly neutral." Mass. Adv. Sh. (1977) at 909, 363 N.E. 2d 474, 482. The presence or absence of discriminatory intent is not relevant under § 1464(h). The use of different measures as the basis of tax inevitably produces differences in the taxes payable. Section 1464(h) cannot be read to permit the use of separate and unequal standards. If, for example, the Massachusetts statute imposed a tax on deposits only of State institutions while Federal associations were taxed only on income, the statute, although neutral, would be outside the scope of § 1464(h). The concurrent use of a Federal standard and a different state standard is not authorized. Such standards preclude comparison. Even if the state statute were wholly neutral in its use of separate standards for imposition of the tax, fortuitous comparative tax burdens on state and Federal institutions are not within the design of § 1464(h). As stated in another case involving different measures of tax:

> If in a conceivable comparison between a domestic and a foreign corporation it should turn out that the foreign corporation paid no more or less than a domestic the result would be fortuitous; "the act has no tendency to produce equality; and it is of such a character that there is no reasonable presumption that substantial equality will result from its application."
>
> *Sneed* v. *Shaffer Oil & Refining Co.*, 35 F. 2d 21, 24 (8th Cir. 1929) (citation omitted).

D. The Massachusetts Statute Violates the Commerce Clause by Its Failure to Provide for Apportionment of Income Derived from Other States.

The Massachusetts Court conceded that Mass. G.L. c. 63, § 11 fails to make any attempt to distinguish between income received from activities within the State and activities outside the State. Mass. Adv. Sh. (1977) at 907, 363 N.E. 2d 474, 481. The Court further acknowledged that "*collectively* the associations invest a substantial portion of their funds (about 29% in 1974) in mortgage loans secured by real estate located in other States," but upheld the statute on the ground that "the record is devoid of any information with respect to the contacts of any *individual* Federal savings and loan association in any other jurisdiction." *Id.* at 907-908, 363 N.E. 2d 474, 482 (emphasis added). This distinction between the collective and individual activities of the Associations is without substance. A significant number of individual associations must necessarily be in the business of making out-of-state real estate loans if nearly a third of the Associations' collective assets are invested in such loans.

By their very nature, mortgage loans involve significant contacts with the state in which mortgaged property is located. All states have systems for the recording or registration of mortgages and other instruments which create interests in real property. *See* A.J. Casner, 4

American Law of Property § 17.5, n. 63 (1952). It is a matter for judicial notice that sound banking practice requires that mortgages be recorded. It is inconceivable that the Associations might have failed to record mortgage loans representing 29 percent of their assets. Moreover, an extensive program of mortgage investment must inevitably have resulted in periodic foreclosures. The use of a state's recording system and foreclosure procedures establishes a direct nexus between the activities of the associations and the recording state. *See, National Geographic Society* v. *California Board of Equalization*, 45 U.S.L.W. 4343 (April 4, 1977) (indirect benefits provided by police and fire departments establish power to tax). Therefore, the decision of the Massachusetts Court, based on the Associations' alleged failure to demonstrate that other states have the power to tax their activities, ignores reality and is clearly erroneous.

The Associations, by showing that they derive significant income from other states and that other states have the power to tax those activities, have demonstrated a substantial risk of double taxation. Such a risk will invalidate an unapportioned tax on gross receipts. *See, e.g., Standard Pressed Steel Co.* v. *Department of Revenue of Washington*, 419 U.S. 560 (1975); *General Motors Corp.* v. *Washington*, 377 U.S. 436 (1964); *Gwin, White & Prince, Inc.* v. *Henneford*, 305 U.S. 434 (1939). No matter what label is used to describe the tax imposed by § 11, the fact is that no deduction is allowed for the major expense of the Associations, *viz.* payments to members. For purposes of the Commerce Clause, the tax must be considered to be on unapportioned gross receipts and is, therefore, invalid.

E. The Use of Separate and Unequal Standards for Measuring Deductions for Required Additions to Reserves Violates the Due Process Clause and Equal Protection Clause.

On its face, Mass. G.L. c. 63, § 11 appears to treat State-chartered banks and Federal associations equally. In operation, however, the statute makes a distinction which is arbitrary, unreasonable and much to the detriment of the Federal associations. The reserve deduction allowed State-chartered banks is determined by the legislature and has remained fixed since the statute was enacted in 1966. The reserve deduction allowed Federal associations is determined by Congress and the Federal Home Loan Bank Board and has been repeatedly adjusted to reflect goals wholly unrelated to tax considerations.

The staute thus distinguishes between the Federal associations and State-chartered banks despite the fact that they are "similar" for purposes of 12 U.S.C. § 1464(h). *United States* v. *State Tax Commission*, 481 F. 2d 963, 968 (1st Cir. 1973). The use of totally different methods for computing the same deduction for members of the same class under the same tax statute violates the due process requirement of *International Shoe Co.* v. *Washington*, 326 U.S. 310 (1945), that economic regulation not be "unreasonable, arbitrary or capricious." *Id.* at 319. Moreover, it violates the equal protection requirement that a law must apply equally to all those within appropriate classifications. *See, e.g., McLaughlin* v. *Florida*, 379 U.S. 184, 190 (1964).

Conclusion.

The tax sustained by the Massachusetts Court represents a significant additional cost of home financing and ownership The current estimate of annual cost is two million

dollars in Massachusetts alone. The search for additional sources of revenues by the several states has been well publicized. As a consequence, it may be anticipated that the Massachusetts approach is likely to be pursued in the several states. In Appellants' view, the Massachusetts approach is unsound and represents a serious threat to the well-being of the Federal instrumentalities and the national policies fostered by them.

Necessarily, serious interpretive problems exist where the Congressional grant to the states of authority to tax is contained in only one sentence. Despite the 44 year existence of § 1464(h), little, if any, authority exists which indicates the extent to which state taxation is permitted, as opposed to beng prohibited, by the Federal enactment. Massachusetts has adopted an approach which authorizes taxation of Federal and state institutions on bases which are not comparable, imposes a stringent burden of proof of factual competition, and, contrary to the intent of the Federal statute and the opinion of this Court, permits adverse discriminatory treatment of Federal associations.

Probable jurisdiction should be noted and the decision of the Supreme Judicial Court of Massachusetts should be reversed.

Respectfully submitted,

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Appendix A.

FIRST FEDERAL SAVINGS AND LOAN ASSOCIATION OF BOSTON & others[1] *v.* STATE TAX COMMISSION & another.[2]

SUFFOLK. November 4, 1976. - May 3, 1977.

CIVIL ACTION commenced in the Superior Court on April 16, 1975. [Case No. 641.]

The case was reserved and reported by *Hallisey*, J., to the Appeals Court. The Supreme Judicial Court granted a request for direct review.

Chester M. Howe for the plaintiffs.

Howard Whitehead, Assistant Attorney General, for the defendants.

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[1] The other plaintiffs are: Boston Federal Savings and Loan Association; Colonial Federal Savings and Loan Association; Security Federal Savings and Loan Association of Brockton; Second Federal Savings and Loan Association; Freedom Federal Savings and Loan Association (formerly First Federal Savings and Loan Association of Worcester); Union Federal Savings and Loan Association of Boston; Metropolitan Federal Savings and Loan Association (merged into Metropolitan Savings Bank which in turn merged into Union Warren Savings Bank); Bay State Federal Savings and Loan Association; First Federal Savings and Loan Association of Fall River; First Federal Savings and Loan Association of Cape Cod; First Federal Savings and Loan Association

WILKINS, J. The plaintiffs are all the Federally chartered savings and loan associations (associations) in the Commonwealth. They seek a declaratory judgment concerning various aspects of the excise which they are required to pay pursuant to G.L. c. 63, § 11(*a*)(1), and § 11(*b*)(1), the significant portions of which are set forth in the margin.[3]

of Lowell; Family Federal Savings and Loan Association (formerly Fitchburg Federal Savings and Loan Association); Natick Federal Savings and Loan Association; Union Federal Savings and Loan Association; Plymouth Federal Savings and Loan Association; Revere Federal Savings and Loan Association; Middlesex Federal Savings and Loan Association; Winter Hill Federal Savings and Loan Association; Waltham Federal Savings and Loan Association; Mutual Federal Savings and Loan Association of Whitman; First Federal Savings and Loan Association of Attleboro; Edward Everett Federal Savings and Loan Association; Scituate Federal Savings and Loan Association; Milford Federal Savings and Loan Association; Monument Federal Savings and Loan Association; Leader Federal Savings and Loan Association; Foxboro Federal Savings and Loan Association; People's Federal Savings and Loan Association; Bay Colony Federal Savings and Loan Association; Montello Federal Savings and Loan Association of Brockton (merged into Home Federal Savings and Loan Association); Home Federal Savings and Loan Association; Home Owners Federal Savings and Loan Association; and Northeast Federal Savings and Loan Association (merged into First Federal Savings and Loan Association of Worcester, now named Freedom Federal Savings and Loan Association).

[2] The Commissioner of Corporations and Taxation is also a named defendant.

[3] General Laws c. 63, § 11(*a*)(1), § 11(*b*)(1), and a certain definition, as appearing in St. 1975, c. 684, § 44, read as follows: "*Section 11.* Every savings bank as defined in chapter one hundred and sixty-eight, every co-operative bank as defined in chapter one hundred and seventy and every state or federal savings and loan association located in the commonwealth shall pay to the commissioner an annual excise equal to the following; (*a*) on or before the twenty-fifth day of the seventh month of the taxable year, there shall be paid (1) six hundred twenty-seven one thousandths per cent of a reasonable estimate of its net operating income, as hereinafter defined, for the taxable year, . . . (*b*) on or before the twenty-fifth day of the first month following the close of the taxable year, there shall be paid (1) one and two hundred fifty-four one thousandths per cent of its net operating income, as hereinafter defined, for the taxable year, less the estimated amount previously paid with respect to such income, ...

"For the purpose of this section, 'net operating income' shall mean gross income from all sources, without exclusion, for the taxable year, less (*i*) operating expenses, (*ii*) net losses upon assets sold, exchanged or charged off as uncollectible during the taxable year, and (*iii*) minimum additions during the taxable years to its guaranty fund or surplus required by law or the appropriate federal and state supervisory authorities . . . ."

The associations argue that the defendant Commissioner of Corporations and Taxation (Commissioner) has misconstrued G.L. c. 63, § 11, by disallowing interest or dividends paid to members as a deduction in arriving at net operating income subject to the excise. They also challenge the excise in its entirety on several grounds, relying on constitutional arguments and on claims that the imposition of the excise is not authorized by Congress. The associations and the defendants moved for summary judgment. A judge of the Superior Court reserved and reported the case on a record which consists of the pleadings, a stipulation of facts, and an affidavit in support of the associations' motion for summary judgment. We granted the associations' request for direct appellate review. We conclude that none of the associations' arguments has merit.

Since 1966, when the income-based portion of the excise was added to the law (St. 1966, c. 14, § 11), the associations have been challenging the application to them of the income-based portion of the excise. Applications for abatement have been filed by the associations for the years 1966 to 1974, inclusive; those applications have been denied by the defendant State Tax Commission (commission); and

petitions under the formal procedure have been filed with the Appellate Tax Board.[4]

For an understanding of the background of this case, we should note Federal court proceedings which also dealt with the excise imposed on the associations by G.L. c. 63, § 11. In 1970, the United States filed a complaint in the United States District Court, District of Massachusetts, challenging the application of that portion of the excise which was based on the deposits of Federal savings and loan associations. Six of the plaintiff associations intervened in that action. The District Court concluded that the provisions of G.L. c. 63, § 11(*a*)(2)(*ii*), and (*b*)(2)(*ii*), resulted in an illegal disparity of tax treatment between Federal savings and loan associations and local savings institutions. *United States* v. *State Tax Comm'n,* 348 F. Supp. 397, 400 (D. Mass. 1972). The Court of Appeals agreed but vacated and modified the judgment in a respect not involving the District Court's central conclusion. *United States* v. *State Tax Comm'n,* 481 F.2d 963, 970-971 (1st Cir. 1973). The issues involved in that case are not before us here. As the result of the Federal litigation, the associations are exempt from the deposits-based aspect of the excise provided in G.L. c. 63, § 11, and those associations which filed timely applications for abatement have received refunds of all payments of that portion of the excise.

In conjunction with the action commenced by the United States, the six associations which intervened in that action filed another action challenging the income-based aspect of the excise of several grounds. Certain of the issues raised here by the associations were presented to the Dis-

[4] Certain of the associations have not filed timely applications for abatement for all years, but that circumstance is not crucial to our resolution of the issues presented in this case.

trict Court and, as indicated subsequently in this opinion, were rejected. *United States* v. *State Tax Comm'n,* 348 F. Supp. at 400-401. Another issue was not considered because the matter was pending before the commission. *Id.* at 401. On appeal the six associations argued the points raised below and pressed certain additional issues, including Federal and State constitutional claims. The United States did not join in the separate challenges advanced by the six associations. *United States* v. *State Tax Comm'n,* 481 F.2d at 966. The First Circuit Court of Appeals declined to pass on any of the issues raised by the six associations because the "taxpayers have adequate recourse to state courts for a determination of their claims." *Id.* at 972.

The defendants do not contend that, because the associations have not exhausted their administrative remedies before the Appellate Tax Board, a declaratory judgment should not be granted in this case. We agree that this is an appropriate case to deal with on declaratory judgment. The associations raise a broad challenge to G.L. c. 63, § 11, presenting questions of statutory construction and of constitutional law of importance to every Federal savings and loan association in the Commonwealth. Although not all of the questions are pure issues of law, because, as will be seen, in certain respects there are matters of proof involved, the resolution of the issues by a court in the first instance in a consolidated proceeding makes practical sense. In other situations of a somewhat similar nature, we have approved an exercise of discretion to grant a declaratory judgment regarding a tax statute. See *Sydney* v. *Commissioner of Corps. & Taxation,* Mass. , - (1976), and cases cited.[5] We turn then to the various arguments advanced by the associations.

[5] Mass. Adv. Sh. (1976) 2538, 2542-2544.

1. The associations argue that amounts paid members, as dividends or interest, are "operating expenses" which may be deducted in arriving at "net operating income." Section 11 of G.L. c. 63 defines "net operating income" as gross income from all sources less certain items, including "operating expenses." The dispute arises because "operating expenses" are not defined. The Commissioner has taken a consistent position that payments of interest or dividends to members are not "operating expenses" and hence are not allowable deductions.[5]

We are concerned, of course, with what the Legislature intended by the words "operating expenses." The associations rely in part on general accounting principles in support of their position. We see no basis, however, for assuming that the Legislature intended to import accounting practice into its statutory language and thus to permit accounting principles to be the guide to the meaning of the words "operating expenses." See *Ivan Allen Co.* v. *United States,* 422 U.S. 617, 635 (1975).

The parties have recognized that, if an association's obligation to a member were a debt, any periodic payment might be equated to the payment of interest and thus represent an operating expense; whereas, if periodic payments to members were equated to dividends, these payments would not be an expense in the traditional sense and thus not deductible. We are invited, as courts are in Federal tax cases involving this issue, to analyze the interest of a member to determine whether he has an equity interest or whether he is a creditor. See *Estate of Mixon* v. *United States,* 464 F.2d 394, 402 (5th Cir. 1972).

[5] The Commissioner's instruction sheet, applicable to excise returns of savings banks, cooperative banks, Federal savings and loan associations, and State savings and loan associations, states that "[a]mounts paid or accrued to depositors, savers or members, whether designated as interest or dividends, are not allowable deductions."

The relationship between an association and its members has elements common to an ownership status and to a debtor-creditor relationship. The charter of an association refers to account holders in terms of ownership and investment. It describes a holder of a savings account as a member who has (1) a right to vote on the election of directors, and to vote on charter amendments, by-laws, and resolutions, (2) a right to a pro rata distribution of net earnings (as defined) twice a year, (3) a right to withdraw his savings account on thirty days' notice, and (4) a right to a pro rata share of the value of the association's assets in the event of liquidation, dissolution, or winding up of the association. There is no fixed date of maturity of an association's obligation to its members, nor any fixed rate of return. A member's status is subordinate to creditors and, when withdrawal of funds is requested, a holder of a savings account does not become a creditor. These elements tend to demonstrate that a member is an investor, not a creditor.

The Federal enabling legislation states that one purpose of a Federal savings and loan association is to "provide local mutual thrift institutions in which people may *invest* their funds . . ." (emphasis supplied). 12 U.S.C. § 1464(a) (1970). See 12 U.S.C. § 1757(8)(D) (1970), as amended, 12 U.S.C. § 1757(8)(D) (Supp. IV, 1974), authorizing Federal credit unions to "invest" their funds in shares or accounts of Federal savings and loan associations. The Federal decisions concerning the relationship of a member and an association support the position that a member is an investor, not a creditor. See *Porter* v. *Aetna Cas. & Sur. Co.,* 370 U.S. 159, 161 (1962); *id.* at 163 (Douglas, J., concurring); *Wisconsin Bankers Ass'n* v. *Robertson,* 294 F.2d 714, 716 (D.C. Cir.), cert. denied, 368 U.S. 938 (1961). To the extent that the status of a member is determinative of

the question whether a periodic payment to him is a payment of interest or the payment of a dividend, the weight of circumstances supports the conclusion that any payment is more analogous to a dividend to an owner than to a payment of interest to a creditor.[6]

We come back, however, to the question of the meaning of the words "operating expenses." Even accepting our conclusion that the status of a member is more like that of an owner than that of a creditor, arguably the words "operating expenses" are ambiguous. In such a situation the consistent interpretation of a statute, since its enactment, by the agency charged with the administration of the law is entitled to consideration in resolving the ambiguity. See *Board of Educ.* v. *Assessor of Worcester,* Mass. , - (1975),[b] and cases cited. It is true that the Commissioner's interpretation, although highly visible as part of the instructions concerning the preparation of the appropriate excise return, is not expressed in the form of a regulation. We also recognize that the Commissioner's interpretation has been subject to objection from the beginning and, thus, is not a settled view, belatedly challenged. These facts, however, bear on the weight to be given to the Commissioner's position; they do not bar us from giving consideration to the Commissioner's view. See *Rockland Mut. Ins. Co.* v. *Commissioner of Ins.,* 360 Mass. 667, 675 (1971). We conclude that the Commissioner's position was adopted contemporaneously and publicly with the enactment of the statute and has been maintained consistently since. It is entitled to some weight in resolving the statutory ambiguity.

[6] We recognize that account holders have ready access to their funds as a practical matter and it is likely that they think of their interests as substantially equivalent to cash. In this sense, a holder of an account is unlike the owner of a share in a corporation who cannot withdraw his ownership interest from the corporation at will. In particular circumstances State courts have concluded that the hybrid relationship between a depositor in a savings and loan association and the association creates a debtor-creditor relationship. See, e.g., *Mengele* v. *Christiana Fed. Sav. & Loan Ass'n,* 287 A.2d 395, 397 (Del. 1972) (Federal savings and loan association); *Family Sav. & Loan Ass'n Shareholders' Protective Comm.* v. *Stewart,* 241 Md. 89, 96 (1965) (State savings and loan association).

[b] Mass. Adv. Sh. (1975) 2626, 2632-2633.

Our own assessment of the status of a member of a savings and loan association, the views of Congress and Federal courts in assessing the nature of the interest of a member of a Federal savings and loan association, and the Commissioner's interpretation all support the conclusion that dividends and interest paid to members are not "operating expenses" within the meaning of those words in G.L. c. 63, § 11.

2. The associations argue next that the excise imposed by G.L. c. 63, § 11, is invalid because it is not a tax authorized by Congress. A federally chartered savings and loan association is an instrumentality of the Federal government and is immune from State taxation in the absence of congressional authorization. *First Agricultural Nat'l Bank* v. *State Tax Comm'n,* 392 U.S. 339, 340 (1968). *M'Culloch* v. *Maryland,* 17 U.S. (4 Wheat.) 316, 436 (1819). *United States* v. *State Tax Comm'n,* 481 F.2d at 969. A State may impose a tax "on such associations or their franchise, capital, reserves, surplus, loans, or income [no] greater than that imposed by . . . [the State] on other similar local mutual or cooperative thrift and home financing institutions." 12 U.S.C. § 1464(h) (1970). This statutory language seems to be concerned largely with preventing unfair tax discrimination against Federal savings and loan associations. See *Laurens Fed. Sav. & Loan Ass'n* v. *South Carolina Tax Comm'n,* 365 U.S. 517, 523 (1961). The variety of taxes authorized by Congress is very broad. Sub-

sequently, we shall consider the associations' arguments that the Massachusetts tax discriminates against Federal savings and loan associations in violation of 12 U.S.C. § 1464(h) (1970). Here, however, we face the claim by the associations that the Massachusetts excise is not a tax authorized by Congress. The argument is that the excise is an unauthorized tax on gross receipts.

The excise imposed by G.L. c. 63, § 11, is a franchise tax. Originally, the excise on savings institutions was measured solely by the amount of the institution's deposits. St. 1862, c. 224, §§ 4 and 5. We characterized the excise, as originally constituted, as a "franchise tax," a tax on the privilege of doing business in the Commonwealth. See *Provident Inst. for Sav.* v. *Commonwealth,* 259 Mass. 124, 126 (1927), and cases cited. In 1966, income was added to deposits as a measure of the excise. St. 1966, c. 14, § 11. This did not change the nature of the excise. A franchise tax measured in whole or in part by income is not unusual. *State Tax Comm'n* v. *John H. Breck, Inc.,* 336 Mass. 277, 299 (1957) (franchise tax on domestic business corporations under G.L. c. 63, § 32, expressed as an excise measured in part by income). *Commissioner of Ins.* v. *Commonwealth Mut. Liab. Ins. Co.,* 308 Mass. 385, 394-396 (1941) (franchise tax on domestic insurance companies under G.L. c. 63, § 22, expressed as an excise measured by premiums). Congress has authorized a nondiscriminatory franchise tax.

Even if we were to view G.L. c. 63, § 11, as providing a tax on income, we note that the excise is not directed against gross income but rather against "net operating income." The associations' argument that the excise is not a tax on net income relies largely on the claim, already discussed, that payments of interest or dividends are not allowed as a deduction in arriving at "net operating income." Such payments need not be deducted for the purpose of ar-

riving at a tax on income which is authorized by Congress and certainly need not be deducted to arrive at a franchise tax authorized by Congress.[7]

The associations' final contention that the excise is not authorized by Congress relies on the allowance as a deduction from gross income of "minimum additions during the taxable year to . . . [an association's] guaranty fund or surplus required by law or the appropriate federal and state supervisory authorities . . . ." G.L. c. 63, § 11, as appearing in St. 1975, c. 684, § 44. The contention is that the excise under § 11 is not an income tax within the meaning of the authorizing Federal statute because required contributions to a guaranty fund or to surplus are not a true expense, and thus "net operating income," as defined, is not income, but it is something less than income. Without accepting the assumption that such a deduction would change an income tax to something else, we doubt that Congress intended that an excise could not be measured by net income reduced by amounts of income which by law may not be made available, at least immediately, to members or depositors as interest or dividends. In any event, as we have said, the excise is a franchise tax, and the allowance of a deduction from gross income for contributions to a guaranty fund or surplus does not make the excise any less so.[8] There is no showing that the allowance of such a

[7] We should not be understood to imply that a nondiscriminatory tax on gross income is forbidden by 12 U.S.C. § 1464(h) (1970). We need not pass on that point.

[8] In their reply brief the associations seem to argue that § 11 is invalid because the First Circuit Court of Appeals has held unconstitutional the excise on deposits under G.L. c. 63, § 11, as applied to Federal savings and loan associations. *United States* v. *State Tax Comm'n,* 481 F.2d at 970. They point out that the excise still applies to deposits of local savings institutions, thus creating discrimination and a failure to achieve the equality of treatment anticipated by the Legislature. This is not a circum-

deduction causes the franchise tax to fail to reflect fairly the annual benefit of the corporate privileges. See *State Tax Comm'n* v. *John H. Breck, Inc., supra* at 285.

3. The associations argue next that the excise is a gross receipts tax which violates the commerce clause of the United States Constitution. They point out that § 11 makes no distinction between income received from activities within the State and activities outside Massachusetts. The record shows that collectively the associations invest a substantial portion of their funds (about 29% in 1974) in mortgage loans secured by real estate located in other States. The record does not show the extent of the contacts of any association with any other State nor does it show whether, in the circumstances of its business operations, any other State does or could impose a tax or excise on any association. Of course, no other State could impose an excise on an association's privilege to do business in Massachusetts.

We have indicated already that § 11 does not constitute a tax on gross receipts. It is a franchise tax. The associations have not argued or shown that a franchise tax which uses net income of a local savings institution as a measure of the excise runs afoul of the commerce clause. Even if we assume, as the associations argue, that the issue of burdening interstate commerce turns on what other States may do, and not what they do in fact (but see *Standard Steel Co.* v. *Department of Revenue of Wash.*, 419 U.S. 560, 563 [1975]; *General Motors Corp.* v. *Washington*, 377 U.S. 436, 449 [1964]), the associations have not met their burden of establishing that § 11 improperly imposes on interstate commerce. *Norton Co.* v. *Department of Revenue*

stance of which the associations properly may complain. The Federal statute (§ 1464[h]) forbids discrimination against, but not discrimination in favor of, Federal savings and loan associations.

of Ill., 340 U.S. 534, 537 (1951). The tax is not invalid per se and, on this record, we cannot determine that it is forbidden by the commerce clause. See *Complete Auto Transit, Inc.* v. *Brady*, U.S. , n.15 (1977).[e] The record is devoid of any information with respect to the contacts and activities of any individual Federal savings and loan association in any other jurisdiction.

4. We come next to the first of the associations' arguments which assert that § 11 violates the mandate of 12 U.S.C. § 1464(h) (1970) that no tax on a Federal savings and loan association shall be "greater than that imposed" by the State on similar local thrift and home financing institutions. The associations contend that their "net operating income" tends to be greater than that of similar institutions because the deduction available to a Federal savings and loan association for "minimum additions . . . to its guaranty fund or surplus required by law or the appropriate federal and state supervisory authorities . . ." (G.L. c. 63, § 11) is generally lower than the deduction available to a similar State savings institution. Additions to a guaranty fund of a local savings institution are required, in particular circumstances, by statute. G.L. c. 168, § 58 (savings banks). G.L. c. 170, § 38 (coöperative banks). Additions to the reserves of a Federal savings and loan association are prescribed by regulations of the Federal Savings and Loan Insurance Corporation. 12 U.S.C. § 1727(a) (1970), as amended, 12 U.S.C. § 1727(a) (Supp. IV, 1974). Although circumstances may vary from institution to institution and from year to year, we accept the associations' assertion that, generally, the required contributions of a Federal savings and loan association to its surplus are less than those of similarly situated Massachusetts savings and coöperative banks.

[e] 97 S. Ct. 1076, 1084 n.15 (1977).

We recognize that it is the effect of the operation of § 11 which must be assessed in determining whether the requirements of § 1464(h) have been met. *United States* v. *State Tax Comm'n,* 481 F.2d at 969-970. We think that the purpose of § 1464(h) is not frustrated by the circumstance that reserve or guaranty fund requirements differ. The cause of the discrimination is the lower requirements imposed by the Federal regulatory agency on Federal savings and loan associations. The Commonwealth is not the source of the discrimination. The excise statute is wholly neutral. We agree with the conclusion of the United States District Court judge on this issue. *United States* v. *State Tax Comm'n,* 348 F. Supp. at 401, vacated on other grounds, 481 F.2d at 976. The operation of § 11 in conjunction with the less strict reserve requirements applicable to Federal savings and loan associations has not been shown to present a substantial competitive disadvantage. Because of lower reserve requirements, Federal associations tend to have more funds available for immediate distribution to members than similarly situated State institutions. Congress must have recognized that reserve requirements would differ between Federal savings and loan associations and State savings institutions. The possible difference in competitive positions is inherent in the pattern of the Federal legislation.

5. The associations raise three constitutional arguments based on the fact that the allowable deduction for an association's contribution to its surplus is apt to be less than the similar contribution of a State institution to its reserves or guaranty fund.

The operation of the statute does not constitute a denial of due process or equal protection of the laws. There is no fundamental unfairness in the due process sense. Every institution is placed in the same classification for tax pur-

poses, but, even if we were to accept the assertion that the associations are placed in a separate class (because of the action of an agency of the Federal government), such a classification would not be impermissible. Legislative classifications for tax purposes are given wide respect in the face of constitutional challenges. *Beals* v. *Commissioner of Corps. & Taxation,* Mass. , (1976).[d] *Mary C. Wheeler School, Inc.* v. *Assessors of Seekonk,* Mass. , - (1975).[e] *Weinstock* v. *Hull,* Mass. , (1975).[f] *Frost* v. *Commissioner of Corps. & Taxation,* 363 Mass. 235, 248, appeal dismissed for want of substanial Federal question, 414 U.S. 803 (1973). *Austin* v. *New Hampshire,* 420 U.S. 656, 661-662 (1975). *Lehnhausen* v. *Lake Shore Auto Parts Co.,* 410 U.S. 356, 359-365 (1973). *Madden* v. *Kentucky,* 309 U.S. 83, 87-88 (1940).

The fact that the deduction allowed to a Federal savings and loan association is determined by a Federal agency decision concerning reserve requirements is not an unconstitutional delegation of legislative powers in violation of arts. 23 and 30 of the Declaration of Rights of the Constitution of the Commonwealth. This is not a case in which some future Federal law or regulation purportedly is accepted by the Legislature as the law of the Commonwealth. *Opinion of the Justices,* 239 Mass. 606, 612 (1921). In numerous instances a taxpayer's obligation is affected by the conduct of other persons, but those other persons are not exercising the authority of the Legislature to tax. Their action may influence the amount of the tax payable, but the taxing power has not been delegated to them.

The excise imposed by § 11 does not violate the requirement of art. 44 of the Amendments to the Constitution of

[d] Mass. Adv. Sh. (1976) 2053, 2059.

[e] Mass. Adv. Sh. (1975) 2311, 2314-2315.

[f] Mass. Adv. Sh. (1975) 531, 536.

the Commonwealth that taxes "be levied at a uniform rate . . . upon incomes derived from the same class of property." The rate is uniform. The amount of allowable deductions will vary among taxpayers for a variety of reasons, including differences in deductions for contributions to surplus or the guaranty fund. That fact does not make the rate other than uniform. If the associations are placed in a separate classification, and, as we have said, the statute itself makes no such classification, such a classification does not violate art. 44. See *Barnes* v. *State Tax Comm'n,* 363 Mass. 589, 594 (1973).

6. We come then to the second contention of the associations that, because of unfair discrimination, the excise violates 12 U.S.C. § 1464(h) (1970). The excise does not apply to credit unions. From this, the associations argue that the excise is invalid because it is not imposed "on other similar local mutual or cooperative thrift and home financing institutions." There is no question that a credit union is a "local mutual or cooperative thrift and home financing institution." See G.L. c. 171, § 2. The issue is whether a credit union is "similar" to a Federal savings and loan association within the meaning of § 1464(h).

Where the question has been presented, credit unions have been regarded as not similar to Federal savings and loan associations. See *First Fed. Sav. & Loan Ass'n* v. *Connelly,* 142 Conn. 483, 492 (1955), appeal dismissed for want of a substantial Federal question, 350 U.S. 927 (1956) (involving a similar claim under § 1464[h]); *State* v. *Minnesota Fed. Sav. & Loan Ass'n,* 218 Minn. 229, 239-241 (1944); *Manchester Fed. Sav. & Loan Ass'n* v. *State Tax Comm'n,* 105 N.H. 17, 19-21 (1963) (involving a similar claim under § 1464[h]).

The associations argue that this is a question of Federal law and that Massachusetts credit unions are not different.

We have held that a Massachusetts coöperative bank is similar to a Federal savings and loan association because "[b]oth appeal to the same type of investor and to the same class of borrowers," and because such institutions "are in direct competition with each other." *Commissioner of Corps. & Taxation* v. *Flaherty,* 306 Mass. 461, 462 (1940), cert. denied, 312 U.S. 680 (1941). Later we held that Massachusetts savings banks are similar to Federal savings and loan associations. *Springfield Inst. for Sav.* v. *Worcester Fed. Sav. & Loan Ass'n,* 329 Mass. 184, 185, cert. denied, 344 U.S. 884 (1952).

There are significant differences between credit unions chartered in Massachusetts and Federal savings and loan associations located in Massachusetts. The test for similarity is not what each type of institution might do but rather what each does in fact, although we note that credit unions have greater restrictions imposed on them than the other institutions.[9] On this record similarity has not been

[9] In the District Court proceedings in *United States* v. *State Tax Comm'n,* 348 F. Supp. at 400, the judge concluded that the omission of credit unions from the excise was proper because there were "enough statutory differences between the powers, functions and legislative policy behind the creation of credit unions, savings banks, cooperative banks, and savings and loan associations . . . to justify the exclusion of credit unions from the excise." He ruled that there was a lack of similarity for the purposes of § 1464(h) because of "different treatment of credit unions in the nature, powers and duties and purposes of credit unions as contrasted with . . . [the other institutions]."

The major statutory differences are in the power to make loans and in the details of the loans permitted. Compare G.L. c. 171, § 2 (purposes of a credit union are accumulating and investing savings of members and making loans to them for provident purposes), with 12 U.S.C. § 1464(a) (1970) (purposes of Federal savings and loan associations are to provide places where people may invest their funds "in order to provide for the financing of homes . . . "). Compare also G.L. c. 171, §§ 24(A), 24(B)(*a*)(4), 24(B)(*b*)(7), 24(B)(*b*)(8), with 12 U.S.C. § 1464(c) (1970),

established so as to make the excise invalid because it does not apply to credit unions. Credit unions, unlike the other institutions, must give preference to personal loans, particularly to smaller loans, and may make loans only to members. G.L. c. 171, § 24. Although credit unions are authorized to make loans secured by first mortgages on real estate, in practice they invest a far lesser proportion of their funds in real estate mortgage loans than do the institutions subject to the excise. In 1972, the latest year for which complete statistics are shown in the record, credit unions placed 30.1% of their total investments (in dollars) in real estate mortgages. Federal savings and loan associations had 87.7% of their total investments (in dollars) in real estate mortgages. The comparable figure for Massachusetts coöperative banks was 80.4% and for Massachusetts savings banks, 65.3%. Analyzed solely in terms of the distribution (in dollars) of loans between personal loans and real estate loans, the disparity is even more marked. Federal savings and loan associations had almost 98% of their total loans in real estate mortgages; coöperative banks had over 97% of their total loans in real estate mortgages; savings banks had over 95% of their total loans in real estate mortgages. Credit unions, on the other hand, had only about 42% of their total loans in real estate mortgages.

The associations have not shown that credit unions compete substantially with Federal savings and loan associations for the same types of investors and the same class of borrowers. Nor have they shown the extent, if any, to which credit unions and Federal savings and loan associations are in direct competition with each other. See *Com-*

as amended, 12 U.S.C. § 1464(c) (Supp. IV, 1974). The authority of credit unions to make loans on real estate mortgages has recently been enlarged. See St. 1977, cc. 20, 22 (effective June 2, 1977).

missioner of Corps. & Taxation v. *Flaherty*, 306 Mass. 461, 462 (1940). We do not reach the question whether any or all of the associations would be entitled to relief if it were shown that one Federal association was in substantial competition with one or more credit unions. The proper method of measuring similarity may be a collective, rather than an individual, comparison.

7. A declaratory judgment shall be entered in the Superior Court consistent with this opinion.

So ordered.

Appendix B.

COMMONWEALTH OF MASSACHUSETTS
SUPREME JUDICIAL COURT
FOR THE COMMONWEALTH

No. 641

FIRST FEDERAL SAVINGS AND LOAN ASSOCIATION OF BOSTON & others,
Appellants

v.

STATE TAX COMMISSION & another,
Appellees

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

Notice is hereby given that First Federal Savings and Loan Association of Boston; Boston Federal Savings and Loan Association; Colonial Federal Savings and Loan Association; Security Federal Savings and Loan Association of Brockton; Second Federal Savings and Loan Association; Freedom Federal Savings and Loan Association (formerly First Federal Savings and Loan Association of Worcester); Union Federal Savings and Loan Association of Boston; Metropolitan Federal Savings and Loan Association (merged into Metropolitan Savings Bank

which in turn merged into Union Warren Savings Bank); Bay State Federal Savings and Loan Association; First Federal Savings and Loan Association of Fall River; First Federal Savings and Loan Association of Cape Cod; First Federal Savings and Loan Association of Lowell; Family Federal Savings and Loan Association (formerly Fitchburg Federal Savings and Loan Associations); Natick Federal Savings and Loan Association; Union Federal Savings and Loan Association; Plymouth Federal Savings and Loan Association; Revere Federal Savings and Loan Association; Middlesex Federal Savings and Loan Association; Winter Hill Federal Savings and Loan Association; Waltham Federal Savings and Loan Association; Mutual Federal Savings and Loan Association of Whitman; First Federal Savings and Loan Association of Attleboro; Edward Everett Federal Savings and Loan Association; Scituate Federal Savings and Loan Association; Milford Federal Savings and Loan Association; Monument Federal Savings and Loan Association; Leader Federal Savings and Loan Association; Foxboro Federal Savings and Loan Association; People's Federal Savings and Loan Association; Bay Colony Federal Savings and Loan Association; Montello Federal Savings and Loan Association of Brockton (merged into Home Federal Savings and Loan Association); Home Federal Savings Association; Home Owners Federal Savings and Loan Association; and Northeast Federal Savings and Loan Association (merged into First Federal Savings and Loan Association of Worcester, now named Freedom Federal Savings and Loan Association), plaintiffs in the above-captioned case, hereby appeal to the Supreme Court of the United States from the final judgment of the Supreme Judicial Court for the Commonwealth of Massachusetts, entered in this action on May 3, 1977, ordering that a declaratory

judgment be entered in the Superior Court for the County of Suffolk.

This appeal is taken pursuant to 28 U.S.C. §1257(2).

/s/ Chester M. Howe
Chester M. Howe
Counsel for Appellants

[As filed July 20, 1977.]

Appendix C.

MASSACHUSETTS GENERAL LAWS, CHAPTER 63, SECTION 11:

Every savings bank as defined in chapter one hundred and sixty-eight, every co-operative bank as defined in chapter one hundred and seventy and every state or federal savings and loan association located in the commonwealth shall pay to the commissioner an annual excise equal to the following:

(*a*) on or before the twenty-fifth day of the seventh month of the taxable year, there shall be paid (1) six hundred twenty-seven one thousandths per cent of a reasonable estimate of its net operating income, as hereinafter defined, for the taxable year . . .;

(b) on or before the twenty-fifth day of the first month following the close of the taxable year, there shall be paid (1) one and two hundred fifty-four one thousandths per cent of its net operating income, as hereinafter defined, for the taxable year, less the estimated amount previously paid with respect to such income . . . .

For the purpose of this section, "net operating income" shall mean gross income from all sources, without exclusion, for the taxable year, less (*i*) operating expenses, (*ii*) net losses upon assets sold, exchanged or charged off as uncollectible during the taxable year, and (*iii*) minimum additions during the taxable years to its guaranty fund or surplus required by law or the appropriate federal and state supervisory authorities; and "taxable year" shall mean any fiscal or calendar year or period for which the bank is required to make a return to the federal government. Federal and state taxes paid or accrued during the taxable year shall not be deductible in computing "net operating income".

Amended by St. 1971, c. 555, § 26; St. 1975, c. 684, § 44.

Appendix D.

COMPARISON OF STATUTORY POWERS OF FEDERAL SAVINGS & LOAN ASSOCIATIONS, MASSACHUSETTS CREDIT UNIONS, MASSACHUSETTS COOPERATIVE BANKS AND MASSACHUSETTS SAVINGS BANKS

	Federal Savings & Loan Associations	Mass. Credit Unions [1] ref: Mass. G.L. c. 171	Mass. Cooperative banks ref: Mass. G.L. c. 170	Mass. Savings Banks ref: Mass. G.L. c. 168
I. DEPOSITS				
Maximum value of shares and/or savings deposits (exclusive of interest) which may be held by one person in one account.[2]	No Limit [3]	$25,000	$100,000 [4]	$100,000 [5]
Reference		§10	§16	§21(1)
II. INTEREST/DIVIDENDS				
Maximum interest or dividends payable on shares and/or savings deposits (excluding time deposits) after required allocation to guaranty or reserve fund.	5¼ percent	8 percent until guaranty fund equals 15 percent of assets	5¼ percent	5¼ percent
Reference	12 C.F.R. §526.3	§25	Mass. G.L. c. 167 §18B, Reg. of Mass. Com'r of Banks published 10/29/70	Mass. G.L. c. 167 §18B, Reg. of Mass. Com'r of Banks published 10/29/70

NOTES:

[1] Assumes assets of over $4,000,000 and membership in Massachusetts Credit Union Share Insurance Corp. or insurance in full under federal or state law.

[2] Exceptions to these limits are made for deposits of state and municipal funds, charitable organizations, pension trust funds, etc.

[3] Deposits of over $40,000, however, are not insured by Federal Savings and Loan Insurance Corporation. 12 U.S.C. §1728(a).

[4] One person may hold no more than 300 serial shares and no more than the combined total of 1,000 paid up and saving shares in the denomination of $100 or half the foregoing amounts if the denomination is $200.

[5] One person may hold up to $40,000 in a savings account and an amount in a term deposit account such that the aggregate of all his accounts does not exceed $100,000 exclusive of interest.

	Federal Savings & Loan Associations	Mass. Credit Unions [1] ref: Mass. G.L. c. 171	Mass. Cooperative banks ref: Mass. G.L. c. 170	Mass. Savings Banks ref: Mass. G.L. c. 168
III. REQUIRED GUARANTY OR RESERVE FUND				
Minimum guaranty or reserve fund required by statute.[6]	5 percent of deposits [7]	15 percent of assets	10 percent of assets	7½ percent of deposits
Reference	12 C.F.R. §563.13	§19	§38	§58
IV. LENDING LIMITS				
A. First Lien Mortgage Real Estate Loans				
1. Out-of-state real estate falling within statutory lending area	Within 100-mile radius of home office	Within 35-mile radius of credit union office	Within town, closest point of which is within 50 miles of town in which main office of lender is located.	Within town, closest point of which is within 50 miles of town in which home office of lender is located.[8]
Reference	12 U.S.C. §1464(c)	§24(B)(b)(4)	§23	§34(2)

NOTES:

[6] In each case, the applicable statute or regulation allows an institution to meet this requirement over a period of time by setting aside a portion of its earnings each year until the required fund has accumulated.

[7] Article 10 of the charter prescribed by the Federal Home Loan Bank ("FHLB") requires the accumulation of a capital reserve equal to 10% of deposits (12 C.F.R. §544.1); however, the FHLB has authorized this requirement to be stricken from charters (12 C.F.R. §544.8). Consequently, the sole remaining reserve requirement is the requirement to accumulate an insurance reserve until it equals 5% of deposits (12 C.F.R. §563.13).

[8] Investment in out-of-state mortgages within the lending area is limited to 25% of deposits if such mortgages are not insured by a governmental agency or to 35% of deposits if 15% of the mortgages are so insured.

	Federal Savings & Loan Associations	Mass. Credit Unions [1] ref: Mass. G.L. c. 171	Mass. Cooperative banks ref: Mass. G.L. c. 170	Mass. Savings Banks ref: Mass. G.L. c. 168
IV. A. (Continued)				
2. Permitted investments in real estate mortgages outside lending area.	(a) *40 percent of assets* [9] or (b) *no limit* if insured by agency of U.S. Government	None permitted	25 percent of deposits if FHA or VA insured	lesser of book value of loans within lending area or 37½ percent of deposits if FHA or VA insured
References	12 U.S.C. §1464(c)	§24(B)(b)(4)	§24A	§35(11)
B. Maximum Investments in First Lien Real Estate Loans				
1. Total investments in first lien real estate mortgages.	95 percent of deposits [10]	80 percent of shares, deposits guaranty fund, reserve fund and undivided earnings	93½ percent of deposits [11]	90 percent of deposits [12]
References		§24(B)(b)(7)		§34(3)

NOTES:

[9] Investments equal to 20% of assets may be made in first lien real estate mortgages on improved real estate and additional investments equal to 20% of assets may be made in participating interests in such mortgages.

[10] No statutory limit is imposed on investments in first lien real estate mortgages; however, the current requirement that each federal savings and loan association maintain liquid assets equal to 5% of its total net withdrawable accounts, established by the Federal Home Loan Bank Board in 12 C.F.R. §523.11 pursuant to authority granted in 12 U.S.C. 1425a(b), precludes investment of this amount in such mortgages.

[11] No statutory limit is imposed on investments in first lien real estate mortgage; however, the requirement that each Massachusetts cooperative bank maintain a liquidity reserve equal to 6 1/2% of its share liability, imposed by Mass. G.L. c. 170, §40, precludes investment of this amount in such mortgages.

[12] A Massachusetts savings bank may invest an amount equal to 75% of its deposits in uninsured or unguaranteed first lien real estate mortgage loans plus an additional amount equal to 15% of its deposits in insured or guaranteed mortgages.

	Federal Savings & Loan Associations	Mass. Credit Unions [1] ref: Mass. G.L. c. 171	Mass. Cooperative banks ref: Mass. G.L. c. 170	Mass. Savings Banks ref: Mass. G.L. c. 168
IV. B. (Continued)				
2. Maximum individual loan secured by one parcel improved residential real estate (4 families or less and owner occupied)				
(a) Maximum amount of one loan	$55,000	$40,000	$60,000 or 5 percent of guaranty fund, whichever is greater	$50,000 or 1¼ percent of deposits, whichever is greater
References	12 U.S.C. §1464(c)	§24(B)(b)(8)	§24(4)	§35(4)
(b) Maximum amount as percent of fair market value of collateral as determined by investment committees	80 percent if authorized by members [13]	80 percent [14]	80 percent if loan for $60,000 or less; 70 percent if loan for more than $60,000	80 percent [15]
References	12 C.F.R. §545.6-1(a)(i)	§24(B)(a)(3)	§24(3)	§35(4)

NOTES:

[13] 90% and 95% loans are authorized if the maximum amounts of the loan are $36,000 and $30,000 respectively. Greater percentages and longer terms are available if the loans are guaranteed or insured. 12 C.F.R. §545.6-1.

[14] 90% loans are authorized if real estate is for one or two-family residence, the term is 25 years and the maximum amount of the loan is $30,000. §24(B)(a)(4).

[15] 90% loans are authorized if the term of the loan is 25 years.

	Federal Savings & Loan Associations	Mass. Credit Unions [1] ref: Mass. G.L. c. 171	Mass. Cooperative banks ref: Mass. G.L. c. 170	Mass. Savings Banks ref: Mass. G.L. c. 168
IV. B. 2. (Continued)				
(c) Maximum term if fully amortized	30 years	30 years	30 years	35 years
References	12 C.F.R. §545.6-1(a)(i)	§24(B)(a)(3)	§24(2)	§35(4)
C. Maximum Investments in Mortgage Participation Loans [16]	20 percent of assets (insured or guaranteed loans not subject to this limitation)	5 percent of shares, deposits guaranty fund, reserve fund and undivided earnings	20 percent of deposits	20 percent of deposits
References	12 C.F.R. §545.6-7 (c)(1)(iv)	§24(B)(a)(6)	§23(4)	§35(8)
D. Unsecured Personal Loans				
1. Maximum investment in unsecured loans	20 percent of assets [17]	95 percent of assets [18]	10 percent of first $50,000,000 of deposits plus 5 percent of balance of deposits [20]	10 percent of first $50,000,000 of deposits plus 5 percent of balance of deposits [21]
References	12 C.F.R. §545.8	§21 [19]	§26(8)	§37

NOTES:

[16] Loan must be one that the participating lender could have made itself.

[17] Loan must be for repairing, alteration or improvement of real property.

[18] Massachusetts credit unions must give preference to small personal loans. §24. Investments in other than personal loans require approval of the directors. §21.

[19] Requires that at least 5 percent of the total assets of a credit union shall be carried as cash on hand or invested in specified ways.

[20] These lending limits assume bank has assets of at least $5,000,000.

[21] The Massachusetts Commissioner of Banks may waive the 10 percent limitation upon application to permit aggregate loans not to exceed 12 percent of deposits. §37.

	Federal Savings & Loan Associations	Mass. Credit Unions [1] ref: Mass. G.L. c. 171	Mass. Cooperative banks ref: Mass. G.L. c. 170	Mass. Savings Banks ref: Mass. G.L. c. 168
IV. D. (Continued)				
2. Maximum individual loan	$10,000 [17]	$1,500	$4,500 [20]	$6,000
References	12 C.F.R. §545.8(a)(1)(i)	§24(A)(1)	§26(8)	§37
3. Term	15 years [17]	36 months	No limit [20]	No limit
References	12 C.F.R. §545.8(a)(1)(v)	§24(A)	§26(8)	
V. OTHER INVESTMENTS				
1. U.S., state and municipal obligations (including obligations of selected agencies there of).	permitted	permitted	permitted	permitted
References	12 C.F.R. §545.9(e)	§21	§26	§§42, 43
2. Banker's acceptances	not permitted	permitted	permitted	permitted
References	12 C.F.R. §545.9(a)	§21	§26(4A)(c)	§49(2)
3. Deposits in other banks	restricted	permitted	permitted	permitted
References	12 C.F.R. §545.9(a), §545.9-2	§21	§26	§55
4. Listed Securities	not permitted	permitted to extent authorized for savings banks	permitted to extent authorized for savings banks	debt obligations of railroad, telephone, public service

NOTES:

See preceding page.

	Federal Savings & Loan Associations	Mass. Credit Unions [1] ref: Mass. G.L. c. 171	Mass. Cooperative banks ref: Mass. G.L. c. 170	Mass. Savings Banks ref: Mass. G.L. c. 168
V. 4. (Continued)				corporations, stock of banks and insurance companies and other investments on annual legal list, are permitted investments [22]
References	12 C.F.R. §545.9	§21	§26(2) and (2A)	§§44-49, 51
5. Maximum investments in office building	not without prior Federal Home Loan Bank Board approval if aggregate book value of existing such investment exceeds 25% of association's net worth	not in excess of guaranty and other surplus accounts, subject to approval of Mass. Comm'r of Banks	not in excess of guaranty fund, surplus account and unallocated reserves or 3½ percent of assets, whichever less	25 percent of guaranty and surplus fund
References	12 C.F.R. §545.10	§21	§30	§53(1)

NOTES:

[22] To invest in these securities, the bank must have assets of over $5,000,000.

Appendix E.

UNITED STATES of America et al.,
Plaintiffs-Appellees,
v.
STATE TAX COMMISSION et al.,
Defendants-Appellants.

UNITED STATES of America et al.,
Plaintiffs-Appellees,
v.
STATE TAX COMMISSION et al.,
DEFENDANTS-APPELLEES.

First Federal Savings and Loan Association of Boston et al., Intervenors-Appellants.

Nos. 72-1380, 72-1381.

United States Court of Appeals,
First Circuit.

Argued March 8, 1973.

Decided June 28, 1973. [963]

Before COFFIN, Chief Judge, McENTEE and CAMPBELL, Circuit Judges.

LEVIN H. CAMPBELL, Circuit Judge.

These appeals question the validity of Massachusetts taxes [1] on the deposits and [965] income of federal savings and loan associations (hereinafter "federal associations").

[1] The taxes are imposed by M.G.L. c. 63, § 11, which reads as follows:

"Every savings bank as defined in chapter one hundred and sixty-eight, every co-operative bank as defined in chapter one hundred and seventy and every state or federal savings and loan association located in the commonwealth shall pay to the commissioner an annual excise equal to the following:

(a) on or before the twenty-fifth day of the seventh month of the taxable year, there shall be paid (1) one-half of one per cent of a reasonable estimate of its net operating income, as hereinafter defined, for the taxable year, and (2) one-twentieth of one per cent of the average amount of its deposits or of its savings accounts and share capital for the first six months of the taxable year, after deducting from such average amounts (i) its real estate used for banking purposes, valued at cost less reasonable depreciation, and (ii) the unpaid balances on its loans secured by the mortgage of real estate taxable in this commonwealth, or real estate situated in a state contiguous to the commonwealth, and within a radius of fifty miles of the main office of such bank or association, and in the case of a bank or association not previously subject to tax by this commonwealth the unpaid balances on such of its loans secured by the mortgage of real estate located outside of this commonwealth which are outstanding on March first, nineteen hundred and sixty-six, both as of the close of such sixth-month period; and

(b) on or before the twenty-fifth day of the first month following the close of the taxable year, there shall be paid (1) one per cent of its net operating income, as hereinafter defined, for the taxable year, less the estimated amount previously paid with respect to such income, and (2) one-twentieth of one per cent of the average amounts of its deposits or of its savings accounts and share capital for the second six months of the taxable year, after deducting from such average amount (i) its real estate used for banking purposes, valued at cost less reasonable depreciation, and (ii) the unpaid balances on its loans secured by the mortgage of real estate taxable in this commonwealth, or real estate situated in a state contiguous to the commonwealth, and within a radius of fifty miles of the main office of such bank or association, and in the case of a bank or association not previously subject to tax by this commonwealth the unpaid balances on such of its loans secured by the mortgage of real estate located outside of this commonwealth which are outstanding on March first, nineteen hundred and sixty-six, both as of the close of the taxable year.

For the purpose of this section, 'net operating income' shall mean gross income from all sources, without exclusion, for the taxable year, less (i) operating expenses, (ii) net losses upon assets sold, exchanged or charged off as uncollectible during the taxable year, and (iii) minimum additions during the taxable years to its guaranty fund or surplus required by law or the appropriate federal and state supervisory authorities; and 'taxable year' shall mean any fiscal or calendar year or period for which the bank is required to make a return to the federal government. Federal and state taxes paid or accrued during the taxable year shall not be deductible in computing 'net operating income'."

In No. 72-1380, the United States seeks a declaration that the deposits tax, § 11(a)(2)(ii) and (b)(2)(ii), violates § 5(h) of the Home Owners' Loan Act of 1933, 12 U.S.C. § 1464(h).[2] The United States objects to the deduction for loans secured by mortgage of out-of-state real estate "within a radius of fifty miles of the main office" of a particlar bank. M.G.L. c. 63 § 11(a)(2)(ii) and (b)(2)(ii). It contends that the 50-mile limitation causes a "greater" tax upon the federal associations than upon other similar state-chartered banks in violation of § 5(h) because the federal associations, unlike state banks, are empowered by controlling federal law to make out-of-state loans on real estate beyond a 50-mile radius and hence get no deduction for loans beyond that limit. We agree with the district court that the challenged deduction results in an

[2] "No State, county, municipal, or local taxing authority shall impose any tax on such associations or their franchise, capital, reserves, surplus, loans, or income greater than that imposed by such authority on other similar local mutual or cooperative thrift and home financing institutions."

illegal disparity of tax treatment between federal and local banks.

In No. 72-1381, six federal associations challenge the income tax, § 11(a)(1) and (b)(1) on grounds that it violates § 5(h) and various state and federal constitutional provisions. The United States has not joined in this challenge. We conclude, under equitable principles which federal courts normally apply to tax litigants other than the United States, that declaratory relief should have been denied without consideration of the merits.

I. *No. 72-1380 (the Deposits Tax)*

The United States, on behalf of the Federal Home Loan Bank Board, brought a complaint seeking a declaration that § 11(a)(2)(ii) and (b)(2)(ii) (the deposits tax) contravenes § 5(h) and the Supremacy Clause of the federal Constitution.[3] Six federal associations were permitted to intervene and joined in the attack on the deposits tax, contending also that the deposits tax violates the Commerce Clause. They raised other issues, which are the subject of the appeal in No. 72-1381.

On plaintiffs' motions for summary judgment, the district court ruled that the deposits tax violates § 5(h) and the Supremacy Clause because it

> operates in a very real way to bring intense economic pressure to bear on federally chartered banks which it does not bring to bear in any meaning-[966] ful way on state chartered banks because of the fact that

[3] Jurisdiction was founded on 28 U.S.C. § 1345. The United States has standing to sue on behalf of its instrumentalities. *See* United States v. Arlington County, 326 F.2d 929, 931 (4th Cir. 1964); Dept. of Employment v. United States, 385 U.S. 355, 87 S.Ct. 464, 17 L.Ed.2d 414 (1966). It is not disputed that the Home Loan Bank Board, established by Congress as an independent agency with responsibility for the savings and loan system, 12 U.S.C. §§ 1437, 1464, is a federal instrumentality.

> other state legislation severely restricts state chartered banks from making any substantial amount of loans in non-exempt areas.

The court also ruled that the deposits tax interferes with the federal associations' ability to carry out congressional purpose and policies in the lending of money, and that it constitutes "an unreasonable burden on the circulation of loans for home improvements in interstate commerce." United States v. State Tax Comm'n, 348 F.Supp. 397, 400 (D. Mass. 1972). It rendered an amended judgment declaring invalid § 11(a)(2) and (b)(2). The Commonwealth has appealed.

M.G.L. c. 63, § 11(a)(2)(ii) and (b)(2)(ii), as inserted by St.1966, c. 14, § 11 and amended by St.1971, c. 555, § 26, is the latest in a series of taxes on the deposits of Massachusetts savings institutions going back to St.1862, c. 224, § 4. The original deposits tax, which before 1966 was imposed solely on non-federal institutions, was litigated extensively in the 1860's; both the Massachusetts Supreme Judicial Court and the Supreme Court sustained its validity,[4] the latter having stated that a deposits tax was,

> better calculated to effect justice among the corporations required to contribute to the public burdens than any other which has been devised, as its tendency is to graduate the required contributions to the value of the privilege granted.

Society for Savings v. Coite, 6 Wall. 594, 608, 18 L.Ed. 897 (1867). A deduction for loans secured by mortgage of Massachusetts real estate taxable in the Commonwealth

[4] Commonwealth v. The People's Five Cents Savings Bank, 5 Allen 428 (1862); Commonwealth v. Provident Institution for Savings, 12 Allen 312 (1866). Provident Institution v. Massachusetts, 6 Wall. 611, 18 L.Ed. 907 (1867).

was enacted in 1881. St.1881, c. 304, § 8. Its purpose was to avoid double taxation, Massachusetts property owners being subject to local real estate taxes at full, fair cash value. Lexington Savings Bank v. Commonwealth, 252 Mass. 180, 182, 147 N.E. 569, 570 (1925). *See* M.G.L. c. 59, § 38; Bennett v. Board of Assessors of Whitman, 354 Mass. 239, 240, 237 N.E.2d 7, 9 (1968).

In 1966 Massachusetts adopted substantially the present statute, extending the deposits tax to federal associations. For the first time, the deduction for loans upon Massachusetts real estate was supplemented by a deduction for loans within a 50-mile radius on real estate in contiguous states. It is that feature which the federal associations attack as resulting in a "greater" tax upon them.[5] The statute provides for a tax of one-twentieth of one percent upon average deposits and share capital after deducting (i) the bank's real estate used for banking purposes; (ii) the unpaid balances on loans secured by "mortgage of real estate taxable in this commonwealth, or . . . in a state contiguous . . . within a radius of fifty miles of the main office of such bank or association." The deduction is further qualified by a "grandfater clause" deduction allowing a bank or association not previously subject to tax to deduct the unpaid balance on loans secured by real estate outside Massachusetts which were outstanding at the time the tax statute was enacted in 1966.

The federal associations are federally created banks. *Cf.* First Agricultural National Bank of Berkshire County v. State Tax Commission, 392 U.S. 339, 340, 88 S.Ct. 2173,

[5] The federal associations' out-of-state real estate loan area had been increased by Congress in 1964, two years before the present Massachusetts tax statute was enacted, from 50 to 100 miles, with no requirement that the real estate be in a "contiguous" state. *See infra.* The local institutions, in 1966 as now, could not loan on out-of-state real estate beyond, at most, 50 miles. *See infra.*

20 L.Ed.2d 1138 (1968). Chartered and regulated by the Federal Home Loan Board under author-[967] ity conferred in the Federal Home Owners' Loan Act, 12 U.S.C. § 1464, they serve the statutory purpose of providing "local mutual thrift institutions in which people may invest their funds and . . . for the financing of homes." § 1464(a). The latter purpose, described more broadly as the "preservation of home owners and the promotion of a sound system of home mortgage," has been said to affect the welfare of the nation as a whole. First Federal Savings and Loan Association v. Loomis, 97 F.2d 831, 840 (7th Cir. 1938), cert. granted, 305 U.S. 564, 59 S.Ct. 92, 83 L.Ed. 355 (1938); dismissed on motion of counsel for petitioners sub nom. Martin v. First Federal Savings & Loan Ass'n, 305 U.S. 666, 59 S.Ct. 363, 83 L.Ed. 432 (1938). *See* Fahey v. O'Melveny, 200 F.2d 420 (9th Cir. 1952), cert. denied sub nom. Willhoit v. Fahey et al., 345 U.S. 952, 73 S.Ct. 866, 97 L.Ed. 1374 (1953).

The federal associations are closely affiliated with their district federal home loan bank (there are twelve nationally), which may provide them credit. The chairman of the Home Loan Bank Board states in an affidavit that the 4500 savings and loan associations in the nation are "the major mortgage lenders on residential properties," playing "the key role in the housing market" and providing "the largest, most stable source of funds for housing." They hold "44% of all outstanding home mortgages" and serve to promote the national housing policy "to provide for the economical financing of home ownership . . . by facilitating to the extent possible the inter-regional flow of mortgage funds from capital surplus areas to nationwide housing markets located in capital shortage areas."

The federal associations are allowed to "lend their funds only on the security of their savings accounts or on the

security of first liens upon real property within one hundred miles of their home office or within the State in which such home office is located. . . .'' § 5(c). The area limit was so extended from 50 to 100 miles by the Housing Act of 1964, Title IX, Pub.L. 88-560, § 901(a), 78 Stat. 804. The accompanying House Committee report stated:

> The present 50-mile limitation was placed in the statute more than 25 years ago. In the intervening years, the country has experienced a tremendous suburban expansion, the establishment of new road systems and mass transit so that the commuting distance and metropolitan areas have been constantly enlarged. In recognition of these changes, your committee feels that the statutory lending area . . . should be 100 miles. . . .

1964 U.S. Code Cong. and Adm. News, p. 3442. The federal associations are also allowed to make certain investments outside the prescribed geographical areas. *See*, e.g. § 5(h), 12 C.F.R. § 545.6-4.

The ''similar local'' Massachusetts institutions purportedly favored by the area limitation in the deduction provisions of M.G.L. c. 63, § 11 are the savings banks (c. 168), the co-operative banks (c. 170), the savings and loan associations (c. 93, § 34) and the credit unions (c. 171). Excepting the credit unions, the similarity of which is disputed, all are conceded to be ''similar'' to the federal associations. *See* Comm'r of Corporations and Taxation v. Flaherty, 306 Mass. 461, 28 N.E. 2d 433 (1940) (co-operative banks similar).

Massachusetts banks are restricted to real estate loans within the state, and within states contiguous to Massachusetts if such loans are not more than 50 miles from the home office in the case of savings banks, and 25 in that of co-

operatives.[6] Section 34 of M.G.L. c. 93 [968] gives the commissioner of banks the same powers and duties over savings and loan associations as he has over savings banks; the district court inferred from this section that the same restrictions on lending area apply to both kinds of banks. The banks may loan upon security outside the restricted area if the loans are VA or FHA-insured. M.G.L. c. 168, § 35(11); c. 170 § 24A.

The district court found, and we concur, that the area limitation in the deduction provision of the deposits tax results in a violation of § 5(h). It also found a violation of the Supremacy Clause, and appellees further claim a violation of the Commerce Clause. We prefer, however, to rest our decision upon the statutory rather than the constitutional grounds.

It is true that the federal associations, being federal instrumentalities, are immune from state taxation by vir-

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[6] SAVINGS BANKS.

> ''Any such corporation may make . . . loans upon real estate secured by first mortgages.'' M.G.L. c. 168 § 34, first para.
>
> ''Such first mortgages shall be on real estate located in the commonwealth, or in a city or town of a state contiguous to the commonwealth, provided, that such city or town is not more than fifty miles from the town in which the main office of such corporation is located. . . .'' § 34(2).

CO-OPERATIVE BANKS.

> ''Any such corporation may make . . . loans of the following types, upon real estate situated in the commonwealth or situated in a state contiguous to the commonwealth and within a radius of twenty-five miles of the main office of such corporation. . . .'' M.G.L. c. 170 § 23.

Formerly, Massachusetts banks could lend only within the state. *See* M.G.L. c. 168 § 54 (Ter. ed. 1932), c. 170 § 23 (Ter. ed. 1932). In the case of savings banks, the lending limit was first extended by St.1946, c. 256 § 1 to contiguous-state loans within 25 miles, and then by St. 1955, c. 432 § 34(2) to such loans within 50 miles. The co-operatives' limit was extended to contiguous-state loans within 25 miles by St.1950, c. 371, § 23.

tue of the Supremacy Clause, absent specific Congressional authorization. McCulloch v. Maryland, 4 Wheat. 316, 4 L.Ed. 579 (1819); Agricultural Bank v. Tax Comm'n, *supra*, 392 U.S. 339, 88 S.Ct. 2173, 20 L.Ed. 1138. *See* Helvering v. Gerhardt, 304 U.S. 405, 411, 58 S.Ct. 649, 82 L.Ed. 1091 (1938). However, since § 5(h) permits states to tax federal associations, the question is not whether Massachusetts may tax but whether its tax conforms to the statute. Obviously, § 5(h) is to be read in light of the purposes of the Home Owners' Loan Act, and with awareness of the objects of the Supremacy and Commerce Clauses; but we see the latter as providing more a frame of reference than as separate grounds for decision.

The Supreme Court has said that § 5(h) "unequivocally bars discriminatory state taxation of the Federal Savings and Loan Associations." Laurens Federal Savings & Loan Ass'n v. South Carolina Tax Commission, et al., 365 U.S. 517, 523, 81 S.Ct. 719, 722, 5 L.Ed. 2d 749 (1961). Otherwise the Court has not had occasion to interpret the clause. However, the Court has said that a similar clause, 12 U.S.C. § 548, permitting state taxation of national banks,[7] is meant "to prohibit only those systems of state taxation which discriminate in practical operation against national banking associations or their shareholders as a class.'" Michigan Nat'l Bank v. Michigan, 365 U.S. 467, 473, 81 S.Ct. 659, 662, 5 L.Ed. 2d 710 (1961), quoting Tradesmens Nat'l Bank v. Oklahoma Tax Comm'n, 309 U.S. 560, 567, 60 S.Ct. 688, 84 L.Ed. 947 (1940). In *Michigan* the Court also said that the states may not "create 'an unequal and unfriendly competition' with national banks," and that "we are taught that in determining the burden of the tax—its discrimina-

[7] "(b) In the case of a tax on . . . shares the tax imposed shall not be at a greater rate than is assessed upon other moneyed capital in the hands of individual citizens of such State coming into competition with the business of national banks: . . ."

tory character—we look to its *effect*, not its *rate*." 365 U.S. at 473, 475, 81 S.Ct. at 662, 663.

Figures stipulated in the district court show that the 50-mile deduction limit discriminates in "practical operation" and in "effect" against the federal associations. We are not persuaded by Massachusetts' contrary marshalling of [969] the figures. Massachusetts relies on the fact that from 1966-70 the total real estate loan deductions available to federal associations actually comprised a greater percentage of deposits than did deductions available to local institutions. But these figures do not separate out the impact of the "grandfather clause" deductions which are, of course, of diminishing and temporary benefit to the federal associations. (The latter characteristics are reflected in figures showing that the percentage of federal associations' deposits not offset by a deduction has risen from 8.7% to 28.6% since 1966.) After allowance is made for the grandfather clause component, the percentage of deductions to deposits is significantly lower for the federal associations than for the local banks. The federal associations make about 44% of their loans on security of real property outside the 50-mile area. The local institutions make only about 15% of the loans on outside property.[8] We conclude that but for the grandfather clause, the federal associations would have received a substantially lesser deduction against deposits in the 1966-70 period and would have paid a greater tax.

It can be argued that the federal banks are not required to loan on real estate beyond 50 miles. But this argument conflicts with the purposes of the Home Owners' Loan Act as interpreted in light of the Supremacy

[8] The deposits of local institutions are not wholly offset by deductible loans since they may invest in VA and FHA-insured real estate loans outside the 50-mile area, and may make non-real estate loans.

and Commerce Clauses. The federal associations and their conferred powers are part of a Congressional scheme, national in scope, to provide a greater supply and flow of funds for home financing. The associations' authority to lend on real estate within a 100-mile area is part of this distinctively federal answer to a national problem. The Congressional aim may not be stultified by state taxation penalizing federal associations at precisely the point they exercise the greater flexibility conferred by their federal franchise. While the local banks may think it fair to obtain relief from competition in areas foreclosed to them, the housing public is entitled to receive the untrammeled benefit of the wider powers. If the federal associations can achieve tax equality only by restricting their lending areas, the tax is discriminatory.

Moreover, the history of the Massachusetts tax statute suggests that the area limitation was designed to create "an unequal and unfriendly" competition. We perceive no reason—other than the impermissible one of sheltering local institutions—for adoption in 1966 of the 50-mile contiguous-state area limitation. It was then apparent that federal associations could loan more widely; indeed the grandfather clause reflected full awareness of the fact. Federal associations are entitled not to be singled out for special tax burdens; and it makes no difference whether the latter are expressly written into the statute or are tailored, as here, more subtly.[9]

We hold that § 11(a)(2)(ii) and (b)(2)(ii) create a discriminatory deduction which results, within the mean-

[9] If we assume the deduction on out-of-state loans was intended to avoid double taxation, thus placing Massachusetts banks on a parity with out-of-state banks in competing for out-of-state loans, the present tax imposes double taxation on home owners borrowing from the federal associations beyond the exempt areas. Again, the result points to discrimination rather than to promotion of some neutral object.

ing of § 5(h), in a "greater" tax upon the federal associations than upon "other similar" local institutions. We do not attempt to resolve the further argument, raised by the intervenors and rejected by the district court, that the tax also violates § 5(h) because not imposed upon credit unions, said to be "other similar" local institutions. The district court ruled that a credit union was not such a ". . . similar local mutual or cooperative thrift and home financing institution" within § 5(h). *See* Man- [970] chester Federal Savings and Loan Ass'n v. State Tax Comm'n, 105 N.H. 17, 191 A. 2d 529 (1963); First Fed. Sav. and Loan Ass'n v. Connelly, 142 Conn. 483, 115 A.2d 455 (1955); State v. Minnesota Fed. Sav. and Loan Ass'n, 218 Minn. 229, 15 N.W.2d 568 (1944). The credit union argument is not advanced by the United States; it is raised only by the intervenor federal associations. Apart from its being unnecessary to our ruling on the deposits tax, we decline to consider it for reasons set forth below in our discussion of the income tax.

The Commonwealth argues that, if we find the deduction provision invalid, we leave the tax undisturbed and strike only the deduction. The only question before us, however, is whether the deposits tax as it applies to the federal associations is invalid. To declare invalid only the deductions portion of the tax on the federal associations would result in an even greater discrimination upon them than now occurs.

The judgment of the district court, as presently worded, appears unnecessarily broad in that it would invalidate the deposits tax on local as well as federal institutions. We remand with instructions to the district court to modify paragraph (1) of its present judgment and decree to read as follows:

> "Massachusetts General Laws, Chapter 63, Section 11(a)(2) and Section 11(b)(2) are invalid and unen-

forceable as applied to Federal Savings and Loan Associations because said tax provisions are in conflict with and violate the provisions of Title 12, Section 1464(h), of the United States Code."

II. *No. 72-1381 (the Income Tax)*

The six federal associations appeal from the district court's refusal to grant them declaratory relief against the income tax, § 11(a)(1) and (b)(1). After the United States filed its complaint, seeking a declaration against the deposits tax, the associations moved to intervene. Their complaint joined in the attack on the deposits tax; but it further prayed, separately, for declaratory relief against § 11(a)(1) and (b)(1) on grounds that the deduction for required additions to guaranty fund or surplus ((iii), formerly (iv), of the last paragraph) constitutes an unlawful delegation under Art. IV and XXX of the Massachusetts Constitution, and that the non-includability of interest on deposits in the deduction for "operating expenses" ((i) of last paragraph) is an unconstitutional burden on interstate commerce in violation of the Commerce Clause.

The Attorney General of Massachusetts opposed the motion to intervene, contending, among other matters, that the federal associations were barred by the Tax Injunction Act (commonly referred to as the Johnson Act),[10] 28 U.S. C. § 1341, from relief in the federal court. The district court permitted intervention under F.R.C.P. 24(b). In answer to the intervenors' complaint, the Attorney General raised the affirmative defense "that the intervenors have failed to pursue the remedies available to them through the state statutory abatement procedure, suit in

[10] "The district court shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of such State."

the state courts for declaratory relief, or other state remedy."

In its brief on motion for summary judgment, the intervenors raised two contentions not contained in the complaint: that the income tax is discriminatory in violation of § 5 (h), and that the entire § 11 violates § 5(h) because it does not cover credit unions, which the intervenors contended, are "similar . . . institutions" within the meaning of § 5(h).

The district court did not rule on the state constitutional issue raised in intervenors' complaint. It abstained from ruling on the question concerning the deduction of operating expenses because [971] of a pending proceeding before the State Tax Commission.[11] 348 F.Supp. at 401. The district court ruled that the deduction for reserve requirements does not violate § 5(h) because

> [t]here is nothing to preclude the Federal Home Loan Bank Board from altering the minimum guaranty requirements of federal savings and loan associations so as to provide a greater tax shelter to the Federal Savings and Loan associations than is allowed by the application of state law. 348 F.Supp. at 401.

It also ruled that credit unions are not similar institutions within the meaning of § 5(h). 348 F.Supp. at 400.

Appellants raise all these issues and, in addition, new issues under state and federal constitutional law. Various considerations compel us to decline to consider the intervenors' claims. Foremost is the policy against federal declaratory relief against state taxing statutes where taxpayers have adequate recourse to state courts

[11] A stipulation states: "There are pending before the Massachusetts State Tax Commission several applications for abatement filed by Massachusetts federal savings and loan associations raising the issue as to whether such deductions should be allowed."

for a determination of their claims. Great Lakes v. Huffman, 319 U.S. 293, 300-301, 63 S.Ct. 1070, 87 L.Ed. 1407 (1943).

In *Great Lakes* the Supreme Court considered the applicability of the Johnson Act, 28 U.S.C. § 1341, to a suit for declaratory relief against a state tax. The taxpayers sought a declaration that the contribution to the state unemployment insurance fund required of them was unconstitutional. The district court held the tax constitutional, and was affirmed by the Court of Appeals, 43 F. Supp. 981 (E.D.La.1942), 134 F.2d 213 (5th Cir. 1943). The Supreme Court affirmed the judgment of dismissal, "but solely on the ground that, in the appropriate exercise of the court's discretion, relief by way of a declaratory judgment should have been denied without consideration of the merits." Great Lakes v. Huffman, *supra*, 319 U.S. at 301-302, 63 S.Ct. at 1074.

The Supreme Court did not hold that the Johnson Act itself barred declaratory judgments. Rather, its holding rested on cases antedating enactment of the Johnson Act requiring federal courts to withhold equitable relief in suits by taxpayers challenging the validity of state taxes. The Court said:

It is in the public interest that federal courts of equity should exercise their discretionary power to grant or withhold relief so as to avoid needless obstruction of the domestic policy of the states.

"The scrupulous regard for the rightful independence of state governments which should at all times actuate the federal courts, and a proper reluctance to interfere by injunction with their fiscal operations, require that such relief should be denied in every case where the asserted federal right may be preserved without it. Whenever the question has been presented, this Court has uniformly held

that the mere illegality or unconstitutionality of a state or municipal tax is not in itself a ground for equitable relief in the courts of the United States. If the remedy at law is plain, adequate, and complete, the aggrieved party is left to that remedy in the state courts, from which the cause may be brought to this Court for review if any federal question be involved." Matthews v. Rodgers, supra, 284 U.S. [521] 525, 526 [52 S.Ct. 214 at 219, 220] 76 L.Ed. 447.

The considerations which persuaded federal courts of equity not to grant relief against an allegedly unlawful state tax . . . are persuasive that relief by way of declaratory judgment may likewise be withheld in the sound discretion of the court. With due re- [972] gard for these considerations, it is the court's duty to withhold such relief when . . . it appears that the state legislature has provided that on payment of any challenged tax to the appropriate state officer, the taxpayer may maintain a suit to recover it back. In such a suit he may assert his federal rights and secure a review of them by this Court. This affords an adequate remedy to the taxpayer, and at the same time leaves undisturbed the state's administration of its tax. 319 U.S. at 298, 300-301, 62 S.Ct. at 1073, 1074.

The Johnson Act and *Great Lakes* reflect much the same policy respecting state tax collections as applies to federal tax collections. *See* 26 U.S.C. § 7421; Enochs v. Williams Packing Co., 370 U.S. 1, 6, 8, 82 S.Ct. 1125, 8 L.Ed.2d 292 (1962). In both instances, efficient tax collection requires that taxpayers not be able to withhold or cast doubt on taxes already or yet to be collected except through established channels. *See* Enochs v. Williams Packing Co., *supra*, 370 U.S. at 7, n. 6, 82 S.Ct. 1125. The policy is even stronger in dealing with state taxes, since the availability of broad declaratory or injunctive relief in federal courts

would promote forum shopping, inconsistent interpretation of state laws, and confusion as to the effect of such judgment on taxes already collected.

In Samuels v. Mackell, 401 U.S. 66, 91 S.Ct. 764, 27 L.Ed.2d 688 (1971), the Supreme Court reaffirmed the validity of *Great Lakes*. There, the question was whether a federal court should declare a state criminal statute unconstitutional during the pendency of criminal proceedings. Again, the Court affirmed the lower court's judgment dismissing the complaint, "but solely on the ground that, in the appropriate exercise of the court's discretion, relief by way of declaratory judgment should have been denied without consideration of the merits." 401 U.S. at 73, 91 S.Ct. at 768. The Court said:

> The continuing validity of the Court's holding in the *Great Lakes* case has been repeatedly recognized and reaffirmed by this Court. *See* e.g., Macauley v. Waterman S.S. Corp., 327 U.S. 540, 545, n. 4 [66 S.Ct. 712, 714] 90 L.Ed. 839 (1946); Ott v. Mississippi Barge Line, 336 U.S. 169, 175 [69 S.Ct. 432, 435] 93 L.Ed. 585 (1949); Public Serv. Comm'n v. Wycoff Co., 344 U.S. 237, 253 [73 S.Ct. 236, 245] 97 L.Ed. 291 (1952) (Douglas, J., dissenting); Allegheny County v. Mashuda Co., 360 U.S. 185, 189 [79 S.Ct. 1060, 1063] 3 L.Ed.2d 1163 (1959); Enochs v. Williams Packing Co., 370 U.S. 1, 8 [82 S.Ct. 1125, 1129] 8 L.Ed.2d 292 (1962). Although we have found no case in this Court dealing with the application of this doctrine to cases in which the relief sought affects state criminal prosecutions rather than state tax collections, we can perceive no relevant difference between the two situations with respect to the limited question whether, in cases where the criminal proceeding was begun prior to the federal civil suit, the propriety of declaratory and injunctive relief should be judged by essentially the same standards. In both situations deeply rooted and long-settled principles of equity have narrowly restricted the scope for federal intervention, and ordinarily a declaratory judgment will result in precisely the same interference with and disruption of state proceedings that the long-standing policy limiting injunctions was designed to avoid.
> 401 U.S. at 71-72, 91 S.Ct. at 767.

Thus, strong authority requires federal courts to withhold declaratory relief "without consideration of the merits" where taxpayers have a "plain, adequate and complete" remedy for their grievance in state courts. Such a remedy is available here. Abatement proceedings before the State Tax Commission may be initiated under M.G.L. c. 63 § 51, made applicable to § 11 [973] taxpayers by § 18A. From there lies appeal to the Appellate Tax Board, M.G.L. c. 63 § 71, c. 58A, §§ 7, 7A, 8, and from there appeal to the Supreme Judicial Court, M.G.L. c. 58A § 13. If a decision from the Tax Commission is not forthcoming within three months of the filing of application for abatement, "it shall then be deemed to be denied and the taxpayer shall have the right at any time within three months thereafter, to take any appeal from such denial to which he may be entitled by law. . . ." M.G.L. c. 58A § 6. In addition to the abatement remedy, a taxpayer may challenge a tax by a suit for declaratory relief. M.G.L. c. 231A, §§ 1, 2. *See* Massachusetts Ass'n of Tob. Dist. v. State Tax Comm'n, 354 Mass. 85, 88, 235 N.E.2d 557, 559 (1968); Stow v. Comm'r of Corporations & Taxation, 336 Mass. 337, 339, 145 N.Ed.2d 720, 721 (1957). Amounts are abated with interest. M.G.L. c. 58A § 13.

We believe these procedures afford intervenors here a "plain, adequate and complete" means of resolving any

issues, federal as well as state, they wish to raise.[12] *Great Lakes, supra,* 319 U.S. at 297, 63 S.Ct. 1070; Helmsley v. Detroit, 320 F.2d 476, 478-480 (6th Cir. 1963); Houston v. Standard Triumph Motor Co., 347 F.2d 194, 199 (5th Cir. 1965), cert. denied, 382 U.S. 974, 86 S.Ct. 539, 15 L.Ed.2d 466 (1966); American Commuters Ass'n v. Levitt, 405 F.2d 1148, 1152 (2d Cir. 1969). *Cf.* Hillsborough v. Cromwell, 326 U.S. 620, 624, 626, 66 S.Ct. 445, 90 L.Ed. 358 (1946).

While the Commonwealth has not urged that we refrain from deciding the § 5(h) claim as it relates to the income tax, it has cited *Great Lakes* for more limited purposes both here and below; and its pleadings raised the question we now consider. In view of the Supreme Court's statement that it is the "duty" of federal courts to withhold declaratory relief in appropriate situations, *Great Lakes, supra,* 319 U.S. at 300-301, 63 S.Ct. 1070, we do not regard the Commonwealth's failure to press fully the issue here as a bar to our following the admonitions of *Great Lakes* and cases following.[13] We are not confronted with a case

[12] State courts have concurrent jurisdiction with the federal courts in the enforcement of federal law, absent a vesting of exclusive jurisdiction in the federal courts. Claflin v. Houseman, 93 U.S. 130, 136, 23 L.Ed. 833 (1876); *see* Testa v. Katt, 330 U.S. 386, 67 S.Ct. 810, 91 L.Ed. 967 (1947). Section 5(h) of the Home Owners' Loan Act has already been applied once by the Massachusetts Supreme Judicial Court to hold invalid a state taxing scheme. Comm'r of Corporations and Taxation v. Flaherty, *supra. See also* Agricultural National Bank of Berkshire County v. State Tax Comm'n, 353 Mass. 172, 229 N.E.2d 245 (1967), rev'd, 392 U.S. 339, 88 S.Ct. 2173, 20 L.Ed.2d 1138 (1968).

[13] In *City of Houston, supra,* Chief Judge Brown writing for the majority said that "it is inconceivable that the Supreme Court intended [in *Great Lakes*] to allow any discretion to grant declaratory relief where adequate state remedies were available." 347 F.2d at 199. We do not, however, need to decide the question presented there, whether, despite the fact that the *Great Lakes* issue was not presented below, the Court of Appeals could properly vacate the judgment for taxpayers under the doctrine of that case. Here, the Attorney General did urge below that the court withhold relief on grounds that an adequate state court remedy existed.

which was exhaustively tried below, where our failure to act, besides disappointing litigants, might lead to a waste of judicial resources. The factual record on the income tax claims is nonexistent and, indeed, quite unsatisfactory for decision of the delicate questions raised. We have neither evidence, agreed facts, nor lower court findings showing the tangible impact and operation of the challenged tax.

That the federal associations have been permitted to intervene in the United States' action, and that the United States' claim has been sustained, do not alter the requirement that the consideration of intervenors' claims regard [974] ing the income tax be withheld. They and the United States stand on different footing as litigants in federal courts seeking to interfere with state taxing schemes. The United States itself is not barred by the Johnson Act from obtaining relief against state taxes in the federal courts. Dept. of Employment v. United States, *supra,* 385 U.S. 355, 358, 87 S.Ct. 464, 17 L.Ed.2d 414 (1966); United States v. Arlington County, 326 F.2d 929, 931 (4th Cir. 1964). *See also* United States v. Bureau of Revenue of the State of New Mexico, 291 F.2d 677, 679 (10th Cir. 1961); United States v. Woodworth, 170 F.2d 1019 (2d Cir. 1948); City of Springfield v. United States, 99 F.2d 860, 862 (1st Cir. 1938), cert. denied 306 U.S. 650, 59 S.Ct. 592, 83 L.Ed. 1049 (1939); United States v. Livingston, 179 F.Supp. 9, 11-12 (E.D. S.C.1959), aff'd, 364 U.S. 281, 80 S.Ct. 1611, 4 L.Ed.2d 1719 (1960). These cases rest in part on the proposition that, absent a strong contrary legislative purpose, the Johnson Act should not bar the United States from access to its own courts of equity, when it seeks to assert its own interest or that of its own instrumentalities.

See United States v. Livingston, *supra,* 179 F.Supp. at 11-12; United States v. Arlington County, *supra,* 326 F.2d at 931, 932-933. Likewise, the equitable doctrine of *Great Lakes* should not deny relief to the United States when it seeks to implement federal policy.

But the intervenors can get no benefit from the presence of the United States. It did not challenge the income tax, and has not joined in the intervenors' complaint or appeal. They are in a different posture than the co-plaintiffs in Dept. of Employment v. United States and other cases cited *supra,* where the non-government party asserted the same claims as the United States.[14] We have found only one case where an instrumentality of the United States—an Indian tribe—suing without the aid of the United States has had its claims for relief considered, notwithstanding the Johnson Act. Agua Caliente Band of Mission Indians v. County of Riverside, 442 F.2d 1184, 1186 (9th Cir. 1971), cert. denied 405 U.S. 933, 92 S.Ct. 930, 30 L.Ed.2d 809 (1972). But that was not a case where the United States had clearly passed up the opportunity to challenge the particular state taxing scheme. Moreover, involving as it did a suit by a party having a unique place in federal law, we see no reason to extend it to all situations where an instrumentality brings a suit against a state or local taxing scheme independently of the United States. The 4500 federal associations, while entitled to wear the mantle of "federal instrumentalities", have many of the characteristics

[14] In United States v. Arlington County, *supra,* 326 F.2d at 932-933, the court said:

> Here we find that the interest of the national government in the proper implementation of its policies and programs involving the national defense is such as to vest in it the non-statutory right to maintain this action. Under these circumstances the incapacity of the individual plaintiff to maintain his action is immaterial since he may find shelter under the Government's umbrella.

of private corporations. They are at the bottom of a three-tiered arrangement headed by the Home Loan Bank Board. It is reasonable, as a prerequisite to by-passing normal state tax collection and litigation channels, that they persuade the Attorney General of the United States, acting on behalf of the Home Loan Bank Board, to join in their claim. We conclude that under the principles of *Great Lakes* intervenors may not obtain declaratory relief against the income tax.

Deciding on this broad ground, we need not rest on any other grounds relating more specifically to several of the issues raised. Plainly, however, some of these claims would have to be dismissed, or not considered, even absent [975] the *Great Lakes* policy discussed above. The federal and state constitutional claims raised for the first time here would not be considered by this Court. Talmanson v. United States, 386 F.2d 811, 812 (1st Cir. 1967), cert. denied 391 U.S. 907, 88 S.Ct. 1658, 20 L.Ed.2d 421 (1968); Securities & Exchange Comm'n v. Milner, 474 F.2d 163, 166 (1st Cir. 1973). The district court did not abuse its discretion in not exercising pendent jurisdiction over the state constitutional claims concerning the income tax. While federal courts have power to determine state law claims joined with federal claims where the different claims "derive from a common nucleus of operative fact", "[t]hat power need not be exercised in every case". United Mine Workers of America v. Gibbs, 383 U.S. 715, 725-726, 86 S.Ct. 1130, 1139, 16 L.Ed.2d 218 (1966). In light of the strong federal policy against interference with state taxing schemes, this was a case where "[n]eedless decisions of state law should be avoided . . . as a matter of comity." *Id.* at 726, 86 S.Ct. at 1139. Similarly, the district court wisely abstained from determining the federal constitutional claim concerning the operating expenses aspect of

the income tax, given the existence of pending state proceedings that might have mooted the constitutional claim. *See* Railroad Comm'n of Texas v. Pullman Co., 312 U.S. 496, 61 S.Ct. 643, 85 L.Ed. 971 (1941); Askew v. Hargrave, 401 U.S. 476, 91 S.Ct. 856, 28 L.Ed.2d 196 (1971).

The declaratory judgment entered by the district court on August 9, 1972, is set aside. A modified judgment is to be entered, clause (1) of which to be worded as set forth earlier in this opinion, and clause (2) of which is to be worded as follows:

> (2) All additional relief sought by the intervening plaintiffs is denied without consideration of the merits.

So ordered. Costs for appellees in each case. [976]